0

SIR ROBERT PEEL'S ACT

OF

1844,

REGULATING THE

ISSUE OF BANK NOTES,

VINDICATED.

By G. ARBUTHNOT.

LONDON:
LONGMAN, BROWN, GREEN, LONGMANS, AND ROBERTS,
1857.

LONDON:
PRINTED BY HARRISON AND SONS,
ST. MARTIN'S LANE, W. C.

TO THE RIGHT HONORABLE

SIR CHARLES WOOD, BART., G.C.B., &c.

Dear Sir Charles Wood,

The distinguished position which you occupied as Chairman of the Committee of the House of Commons on Banks of Issue, in 1840, and as Chancellor of the Exchequer during the memorable commercial crisis of 1847, will always associate your name with that of Sir Robert Peel, in connection with the Bank Charter Act of 1844. Differing from him generally in political opinions, you were united with that eminent statesman in the views which led to the adoption of the Act, and in the subsequent defence of its principles. Opportunities were afforded me of obtaining an insight into those views, by the circumstance of my having served under you as private secretary in 1847, and also under Sir Robert Peel, in the same capacity,

for several years, including that of 1844,—opportunities which are enjoyed by few, and which I have endeavoured to improve, by subsequent attention to the working of the measure. Being satisfied that misapprehension has arisen in many minds from an imperfect acquaintance with the facts essential to the formation of a sound judgment on the subject, I am induced, at the present time, when much interest has been excited in the questions at issue, to offer to the public the result of my observations, and to bring under its notice some particulars which have not hitherto obtained general attention.

If I could have persuaded myself that the question would be elucidated by new views or new theories, I should have left to more able hands the duty of laying before the world the principles by which the currency of this country ought to be regulated. My task, however, is a humbler one. I only profess to follow the footsteps of the great writers on political economy, headed by Dr. Adam Smith and Mr. Ricardo; and to be guided by the researches of men, like Lord Overstone and Mr. Norman, who unite practical experience with sound theoretical knowledge. But although the principles which I advocate are not new, and are simple in character, the ramifications of the subject are wide and its details intricate. In follow-

ing these ramifications many writers have perplexed themselves and their readers by founding theories on exceptional circumstances. Others have been led astray by statistics—the characteristic form of modern research—which, according to the use that may be made of them, may become either the guide or the snare of the political inquirer. Without doubt accurate statistical returns are invaluable to those who carefully study them; but the information which they afford consists only of a great accumulation of facts: and, as zealous controversialists have ever been prone to seize the first fact that suits their argument, so with the growth of statistics has sprung up the disposition to misapply them. Few have the opportunity of threading their way through the mass of details which it is often necessary to investigate in order to detect a single error; and some service may be rendered to truth and science by a patient inquiry into assertions and arguments which, though lightly adopted, are often specious and captivating. The object which I have in view is to unravel the tangled web of fallacious reasoning, which is the consequence, if not the cause, of a careless and confident reference to facts, and to prove that candid investigation will confirm the principles on which the Act of 1844 is founded.

In the hope that my labours may not be altogether fruitless in promoting those sound principles of monetary science which you have advocated, I beg leave to dedicate this tract to you ; and to subscribe myself, with sentiments of great respect and esteem,

Dear Sir Charles,

very faithfully yours,

G. ARBUTHNOT.

January 1857.

SIR ROBERT PEEL'S ACT OF 1844,

&c., &c.

SECTION I.

INTRODUCTION.—THE OBJECT OF THE ACT OF 1844.—SUMMARY OF THE OBJECTIONS TO ITS PROVISIONS RAISED BY ITS OPPONENTS.

THE object of the Bank Charter Act of 1844 was, so to regulate the issue of bank notes, that the paper money, conjointly with the metallic money of the country, should, in all respects, be governed by those natural laws by which the amount of money would be determined if the currency were entirely metallic. With this view it prevents the establishment of any new banks of issue; imposes a limit on the amount of notes to be created on the credit of securities; and provides that any notes in addition to the amount of that limit shall represent bullion deposited in the Bank of England.

The Act was followed by the Acts of 1845, which are a corollary to it, for the regulation of the paper money of Ireland and Scotland, on a similar principle, but on a modified plan. The Act of 1844 precluded the establishment of any additional banks of issue in the United Kingdom. The Acts of 1845 extended to Ireland and Scotland the provision by which the amount of notes to be issued on credit by then existing banks of issue is restricted to the amount of their average circulation at a specified date. This amount is usually termed the "fixed issue" of those banks.

Unlike the country banks of England, however, the issuing banks of Ireland and Scotland are empowered to issue notes, in addition to their fixed issue, for an amount equal to the amount of coin held by them.

The effect of these measures is, that the circulation of the United Kingdom must necessarily vary according to the amount of bullion deposited in the Bank of England, and of coin held by Irish and Scotch banks, and the notes which can be issued on the credit of securities being considerably within the amount required for the circulation of the country, even in times of the greatest contraction, each note must necessarily bear in exchange the value of the coin which it represents.

By the advocates of this system it is regarded as a complement of the Act of 1819, by which specie payments were resumed. They consider that, although the principle of the convertibility of bank notes was recognized by that Act, it was imperfectly carried into effect so long as a discretionary power of issue was left to many independent banks. Experience proves that such a power was liable to be abused, and had led to excessive issues in times of excitement, to undue exhaustion of the bullion in periods of pressure, and consequent danger to the convertibility of the note, causing derangement of our monetary system, the failure of banks, and distress throughout the community. Some alleviation of these risks would be attained by placing the control over the circulation in one central body like the Bank of England, yet that institution was itself exposed, from its connection and sympathy with the mercantile body, and its wish, under certain circumstances, to assist the Government, to the temptation of delaying any action upon the circulation in times of pressure, until the reserve of bullion might be reduced to so low an amount as to create alarm and bring the notes of the bank itself into discredit. For these reasons they consider the restrictions imposed by the

Acts of 1844 and 1845 to be essential to the security of our monetary system.

The soundness of these views is questioned by two classes of objectors. The first class consists of those who are opposed not only to the Acts of 1844 and 1845, but to the very principle of the Act of 1819. The second consists of a body of political economists, numbering among them such men as Mr. Tooke, Mr. Fullarton, Mr. James Wilson, and others, whose opinions are entitled to great respect, and who, fully recognizing the principle of the legal convertibility of bank notes, yet consider that the Bank Charter Act is unnecessary for that object, and that it imposes restrictions detrimental to the commercial interests of the country.

It would be a waste of time to repeat the arguments by which the visionary views of the first class of objectors have been refuted. These enthusiasts are beyond the reach of argument themselves, and their reasoning is not calculated to carry any weight beyond the limits of their own circle.

The reasoning of the second class, based on theories less opposed to fundamental principles, leads to conclusions involving questions both of fact and expediency, and demands deeper consideration. Their opinions may be summed up as follows:

(1.) That when legal convertibility of bank notes exists, and the traffic in the precious metals, coined or uncoined, is free and unrestricted, no excess of issue can take place; and that the bank issues, if left to themselves, must necessarily fluctuate in conformity with the principles which govern the supply of the standard metal. That any restraint, therefore, upon the issue of bank notes is unnecessary.

(2.) That, as the action of the Bank of England on the credit of the country is mainly derived from the use of the deposits entrusted to it, in the employment of which its

discretion is necessarily unrestricted, the Act of 1844 leaves it unfettered in that part of its functions in which injudicious management may most affect the public interests; and, in imposing restraint upon its power of issue, interferes only with a discretion which might be exercised with safety, and even with great advantage to the community, in times of difficulty and alarm.

(3.) And, finally, that the soundness of these views has been demonstrated by the mercantile pressure of 1847, which, so far from having been prevented by the operation of the Act of 1844, was greatly aggravated by that measure, and the panic resulting from which was only alleviated by the virtual suspension of the Act.

These views have been recently brought before the public in a pamphlet by Mr. Tooke, in which, with the assistance of Mr. Newmarch, he has condensed and reinforced opinions formerly advanced by him in condemnation of the Act of 1844. They have also been advocated in the "Economist" newspaper, in several articles which appeared in the latter part of the year 1855, extending the line of argument which had been adopted in the same journal during the three years from 1845 to 1847, in a series of essays from the pen of Mr. Wilson, afterwards collected in a volume and published in his name.

It may be observed that the operation of the Act of 1844 on the functions of the Bank of England, as the central and controlling issuing bank of the kingdom, is mainly called in question in these objections; but if it be a sound doctrine that, with legal convertibility of bank notes, the circulation of the country would be self-regulating, it would follow that the privilege of issue might be safely entrusted to a numerous body of bankers, acting independently of each other. The objections, therefore, apply to the restrictions imposed on Issuing Banks in general, as well as to those imposed on the central and controlling establishment.

Although these writers repudiate the fallacies of the school which advocates the inconvertibility of bank notes and rejects a metallic standard of value, they are themselves influenced by theories which, carried out to their legitimate results, would affect many of the received maxims of political economy. In order, therefore, to pave the way for an examination into their peculiar tenets, it will be desirable to state succinctly, in the first instance, the principles by which value is determined, and the precious metals distributed throughout the world, as established by the investigations of Economists of the highest authority. These principles will form the subject of the next section.

SECTION II.

LAWS WHICH REGULATE THE VALUE AND DISTRIBUTION OF MONEY.

As all value is the product of labour, using the term in its widest sense, the natural value of different commodities is derived from the quantity and quality of labour which is employed in producing them. Capital is the accumulation of successful labour, and consists of the food, clothing, materials, machines, buildings, and appliances employed in production, including in the category expenditure incurred in qualifying men for services. The desire for an interchange of the products of industry is a necessary consequence of that mutual dependence which is a condition of human nature, and with the progress of society, and extended division of labour, the motives for this natural trade would augment. The inconveniences of direct barter would then be felt, and there would arise a necessity for the adoption of some common medium of exchange and measure of value. By universal consent gold and silver came to be employed for this purpose.

The causes which gave rise to this use of the precious metals have been so fully investigated by writers on political economy, and are so clearly established, that it is unnecessary to particularize them. It is sufficient to observe that, like other products, the general value of gold and silver is dependent on the labour employed in producing them, and that the circumstance of the amount of labour so employed being less liable to variation than that engaged in other pursuits of industry, combined with the quality of comparative indestructibility, gives to these metals a relative fixity of value, which renders them the best standard that can be obtained by which the value of commodities in general can be measured.

The additional quality which they possess of containing a large value in small bulk, rendered them convenient as a medium of exchange, and this convenience was reduced to its most complete form, when the weight and purity of given portions of them were authenticated by the State in the shape of coins. The essential properties of money thus derived have been clearly defined in the following terms:*—

"1st. That it is a sign or representative of value.

"2nd. That it is a standard of value.

"3rd. That it is an accurate measure of value, from the highest to the lowest degree.

"4th, and as a corollary. That it is in universal demand and forms the general medium of exchange.

"The final result of its possessing these properties is that the civilized part of mankind, at all times and in all places, are willing to receive it to any extent in exchange for all articles which they may wish to sell."

The distribution of gold and silver throughout the world is effected by the natural competition which arises from the desire to acquire that which is universally prized and may always be exchanged for other products. The quantity of these metals which can be obtained by each country will depend on the value of its labour; and the country procuring them will use such portion of them for money as its trade requires.

The value of money is measured by the quantity of commodities and services against which it will exchange. The value depends, like that of all other things, at each particular time, on the demand and supply: increase the supply of money, and the quantity of commodities given in exchange for it will be diminished; diminish the quantity of money, and the quantity of commodities given in

* Letter to Sir Charles Wood, on Money, by G. W. Norman, Esq., 1841.

exchange for it will be increased. In the first case, the money price of commodities will be raised; in the second case it will be diminished.

Prices in general, with a purely metallic circulation, unrestricted in its operation, other things being equal, would then vary with the supply of the metal of which the money is composed, and, according to the natural laws of commerce, the precious metals would flow into those countries in which the greatest quantity of commodities could be obtained for them. In other words, with rising prices, the general supply of those metals remaining the same, there will be a tendency in any given country to an efflux of gold and silver, or with falling prices a tendency to an influx.

As the proportion of the circulating medium to the transactions carried on by it governs prices, it would follow that any artificial limitation on its amount would have the same effect, in this respect, as a limitation on a currency of intrinsic value arising from the natural movement of the precious metals. Token coins, or paper money, may pass current upon this principle, in internal exchange, as the representatives of value which they do not possess in themselves.

An artificial increase in the circulating medium would, on the contrary, have the effect of raising prices; but it is impossible that with legal convertibility, practically fulfilled, that effect can be permanent. Thus, let us suppose the circulating medium to be extended by the use of paper money, or other expedients by which the employment of coin is dispensed with: these will have the same effect, in the first instance, as the introduction of an additional supply of metallic money. If such expedients are employed in substitution for metallic money already in use, a rise in prices bearing a relation to the quantity of money disengaged from its former uses will be the natural result. But by this rise the relation of prices with those of other

countries will be disturbed, and an export of the precious metals will ensue until the equilibrium be restored. Prices will thenceforth be subject to the same range of fluctuations as they would have been liable to before the introduction of means for economizing money; but this important consideration occurs, that in the degree to which the quantity of metallic money, relatively to the value of the transactions carried on, is diminished by these economising expedients, the effect upon prices arising from the action of foreign exchanges on the remaining quantity will be proportionably increased.

Exchange between different countries.

It is unnecessary to particularize the complex but well-understood machinery by which bills of exchange, the silent agents in the adjustment of prices, facilitate the mercantile transactions of the world; but it is important, with reference to some opinions which have been broached on the subject, to define the nature of the value which they are the means of circulating. Setting aside the uses to which securities of this description may be incidentally applied, foreign bills are drawn against credits and represent either debts or advances; but the ultimate means of adjusting the liabilities incurred by their use is generally derived from the value of exported commodities. They are employed for the purpose of effecting payments; and assuming, for the sake of simplicity, a case of direct interchange between two countries, it would follow that when the aggregate amount of transactions to be adjusted between them may be equal, the aggregate amount of the bills drawn by the merchants of each country would be equal. In that case, exchange would be at par, and their mutual engagements would be adjusted by the set-off of the bills of one against those of the other, without the intervention of a money payment. But if the the value of the exports from one country should fall short of the value of the imports from the other, or from any

disturbing circumstances, such as loans or remittances of capital, a balance of payments should be due from one country to the other, that balance would have to be transmitted in specie.

It rarely happens that trade is so evenly balanced as to leave the exchanges at par. The inequalities, when not excessive, are readily adjusted, in the first instance, by the system of buying bills for transmission at a market price, varying according to the demands for payments to the country on which they are drawn. This price can seldom be maintained for any long time at a rate which would exceed the cost of transmitting specie. If the rate of exchange between New York and London were 1 per cent. against this country, a merchant in London might give 101*l.* for a bill on New York representing the value of 100*l.*; but if the adverse rate rose to 1½ or 2 per cent., which would exceed the cost of transmitting specie, he would naturally remit 100 sovereigns in preference to purchasing a bill. The distribution of the precious metals throughout the world is thus brought about by the effect of a natural law, which no ingenuity can evade. It is obvious that if, in times of speculation, an attempt be made to maintain undiminished in amount the circulation of securities which may be accepted as representatives of money, in the face of an adverse exchange, the drain of bullion may proceed, until the last resources of the indebted country are exhausted.

The point to be borne in mind in this discussion is, that though bills of exchange, when used for purposes of commerce, are drawn on the security of floating capital or produce, and, so long as trade is sound, are discharged from the returns of that capital or produce, the obligation incurred is for a money payment, and can only be fulfilled by the payment of money or its equivalent. If the produce realize its expected money price, no difficulty will arise; but if it fail to realize that

price, the merchant must fall back on other resources. What is true with regard to the merchant individually, is true with regard to the nation at large.

In the foregoing summary of the broad principles on which value is determined and money circulated, qualifying circumstances, which must arise in so complicated a subject, have been disregarded. They affect only in a small degree the general argument. It is not necessary, for example, to the elucidation of the subject, to advert to the disturbing influences arising from charges in the shape of seignorage or other restrictions on the issue of coin from mints, or from the varying value of gold and silver relatively to each other. Discrepancies arising from such circumstances are adjusted by the fine calculations of those concerned, and they do not in any respect affect the fundamental principles upon which the question rests.

The principles laid down are those in which all sound political economists are in the main agreed. The subject to be discussed will resolve itself into the question of the extent to which those principles may admit of modification under the system of credit now in operation in this country. Few will deny that the abuses of credit are the main causes of mercantile and monetary derangement; but many are of opinion that credit itself may be employed, without danger to the community, in rectifying or mitigating the consequences of those abuses.

The system of credit and the principles on which it is founded will have to be now considered.

SECTION III.

THE SYSTEM OF MERCANTILE CREDIT.—BANK NOTES.—COMPARED WITH OTHER PAPER CREDITS.—THEIR ESSENTIAL CHARACTER.

ı of
ıtile

UNDER the system of banking established in this country, credit is largely employed by two classes of persons, namely, by the bankers or bill-brokers who lend out the deposits entrusted to them; and by the merchants, manufacturers, agriculturists or others, who, by means of loans obtained from the first class, are enabled to extend their operations and increase their profits. By means of this system, the dead stock, consisting of money, which, without the convenience afforded by banking accommodation, every trader and every wealthy person would be obliged to keep by him for current payments, is converted into active capital, and the use of money is economized by a large portion of the current daily payments and obligations of the community being discharged by means of banker's drafts, transfers of book credits, and other forms of paper credit.

The extent to which the operations of trade are promoted by this liberation of capital, drawn from the common stores of the community, may be conjectured from the amount of deposits in the joint stock banks of London alone, the average of which is stated to be no less than 38,000,000*l.*

The fund at the disposal of bankers, derived from deposits, added to their own capital, consists of money or securities for money; but an indefinite line of argument pervades the reasoning of the objectors to the Bank Act of 1844, which seems to call in question this simple fact. Bills, say they, are drawn on the

credit of capital, and deposits represent capital; therefore it is the amount of available capital, and not of money, that governs the amount of credit which may be given by bankers. The fallacy involved in this theory will be the subject of further discussion; but, as a practical question, there can be no doubt that the ability to turn securities into money, in case of necessity, should form the most important element of a banker's calculations. He is liable to be called upon at any time for the payment in money of the deposits entrusted to him, and the security and success of his transactions will depend on the manner in which he employs the fund at his disposal, so that his advances may be continually returning, and his investments may be of that temporary character which will allow of their being readily realized in the event of a necessity arising for strengthening his reserve. That reserve must consist of money (whether metallic or paper). It is the portion of his fund which is kept in readiness to meet uncertain demands, and its condition affords the test by which a prudent banker will be governed in curtailing or extending his accommodation to traders. The term "hoard" is used by Mr. Fullarton, and adopted by Mr. Tooke, with reference to some supposed portion of a banker's treasure which may be available for use on emergencies; but there is no part of his resources which can be properly regarded in this light. A hoard is a quantity of treasure kept unnecessarily in an unproductive state, and it is contrary to the very principle on which the institution of banking is established to suppose that any part of the deposits entrusted to a banker, which he can prudently and advantageously employ, will be allowed to remain idle in his vaults. So far from its being an object with a prudent banker to maintain a hoard with a view to its being parted with in times of pressure, his general effort will be to strengthen his reserve on the first symptom of approaching difficulties, in order to be

prepared for demands exceeding their usual amount. He will deal more freely with his funds, and give accommodation for longer periods, when no ground exists for such anticipation of increased demands. No illustration can be needed to prove that the ability of banks in general to afford accommodation to the trade of the country must be derived from the money possessed by them or at their command, or, in other words, must depend on the condition of their aggregate reserves and their means of recruiting them. According to the state of these reserves at any time, money, to use the familiar but expressive term of the dealers, will be abundant or scarce, trade will be easy or restricted.

notes. By the issue of bank notes, as the law stood previously to 1844, bankers might enlarge the fund at their disposal for the accommodation of trade; and they might do this with safety to themselves, and without detriment to the public, so long as their issues did not raise the circulation beyond the limit which, under the natural operations of commerce, would otherwise be filled by imported specie. The profits of the banker from this operation would be equal to the interest on the capital relieved from the cost of procuring metallic money, and trade would be benefited by the increased accommodation which he would be thus enabled to afford. This is the extent of the advantage to trade which can be legitimately derived from the use of bank notes, but the State obtains the additional advantage of a saving of the cost of coinage. If bankers had confined their issues to these legitimate objects, the necessity for restraint would not have arisen; but temptation to an abuse of the privilege has generally proved too strong. Unity of action among a large number of competing bodies can seldom be secured; and the facility which the issue of paper money affords of extending credit without immediate cost, offers a strong inducement to an improvident increase of the circulation, which would not exist if

bankers were subject to the previous charge of procuring coin.

The issuer of notes becomes a debtor for the amount of his issues to the public among whom they circulate, and the liability thus incurred entails an additional risk on the depositors. The security both of the public in general and of the depositors would depend on the degree of caution which the banker might exercise in regulating his issues by the state of his reserve, combined with his general prudence in the conduct of his business.

Bank notes so issued without restriction may be considered in the double light of an exercise of credit and of a substitute for metallic money. It is in the former light that they are principally regarded by the opponents of the Bank Act of 1844, who confound them, under the general term "circulation," with other forms of paper credit, such as drafts upon bankers, transfers of book credits, and bills of exchange.

Before we treat of the essential attributes of bank notes, it will be desirable to investigate the character of other paper credits with which they are brought into comparison, and to define, as accurately as the complex nature of the subject will allow, the part which they fulfil in the discharge of monetary functions.

Deposits.

Deposits with bankers and discount houses constitute the principal fund on which the credit system of the country is reared; and by their use, and by the facilities which they afford for the settlement of debts by drafts or the transfer of book credits, the employment of coin or bank notes is entirely dispensed with in most of the important monetary transactions of the country, and in a great proportion also of smaller payments.

The theory on which the growth of book credits is established on a small money basis was first clearly propounded by Mr. Pennington, who showed the manner in which a single deposit might become the source of a pro-

gressive series of credits. As the legitimate profits of a banker are derived from the use of a portion of the money entrusted to him, he would retain in his till only such proportion of a deposit placed in his hands as might be found by experience to afford a sufficient fund for casual payments, and as a reserve against contingent demands. The rest he would employ in advances on bills of exchange, or in the purchase of securities. The amount of the reserve usually held by London bankers has been variously estimated. By some writers it has been placed at no larger an amount than one-tenth of the deposits; and in the keen competition for profit which at present exists, it is probable that, in the case at least of some of the joint stock banks this conjecture may not be far from the truth. Assuming, then, for the sake of argument, that the operation of banking may be safely conducted with so low an amount of reserve, the banker obtaining a deposit of 10,000*l.* would seek to invest 9,000*l.* in some description of securities; but the person acquiring this money by the sale of public securities, or the negotiation of bills of exchange, would employ it for the purposes of his business, and would deposit it with his banker for his use. A second deposit would thus be raised on the original sum, and would give rise to a further proceeding of a like character, and to others in succession. Thus, with the progress of the banking system, book credits would come to represent the main fund of commercial wealth.

Great, however, as their amount is, there is still a natural limit beyond which they cannot be carried. We have seen how deposits may be multiplied until the money on which they are founded bears but a small proportion to the fund created; but the process must stop at the point at which banking expedients may be brought into full operation. These expedients dispense with the use of money, but they do not create it.

There is a counteracting influence in continual opera-

tion, which prevents the indefinite extension of credit. While deposits are created on one hand, they are diminished on the other by the daily demands for the payment of wages and services, and for other requirements of trade; and, in times of difficulty, the general fund is subject to curtailment, not only from the withdrawal of sums for the purpose of procuring bullion for exportation, but from the pressure on the resources of the numerous body of depositors. The aggregate fund of the deposits can at no time exceed the amount which the available capital of the country affords.

Mr. Tooke and other writers who concur in his opinions, admit this principle in terms, but their peculiar reasoning regarding capital seems to imply that the fund at the disposal of bankers is derived from some other source than the coin and notes which supply the circulation of the country; as if there were a fundamental difference between the credit payable on demand and the money in which it is paid, and as if the expedients by which money payments are dispensed with altered the principle by which prices are regulated. The reasoning must be fallacious which leads to the conclusion that the essential character of money engagements can be in anywise affected by the substitution of an inexpensive for a costly medium of payment, or by the intervention of a refined system of credit. Money capital is a command over existing floating capital, measured or represented by money, and this command is the same, whether the capitalist holds his treasure in coin or bank notes, or has a credit for it in the books of a solvent banker.

On the other hand, securities of all descriptions are charges on future profits. They consist of fixed charges, such as the public stocks, mortgages, &c.; or of credits raised on the anticipated returns of merchandise, or with a view to ulterior profits from agricultural improvements, the construction of machinery and factories, shipbuilding,

railway enterprises, or other undertakings. It is from the demands for floating capital, for uncertain and often speculative investments of this description, that the great struggles in the money-market arise. When trade is active, profits large, and the returns quick, those who engage in such adventures can afford to give a high price for the command of money. When, on the other hand, floating capital is abundant, and the opportunities for its employment are slack, those who possess it must be content with a smaller return for the loan of it. The price paid for the use of money is a share of anticipated profits, in the shape of interest, and the rate of interest is governed by the extent of the demands for the loan of capital, and the quantity at the same time available. The circumstance that money is the usual form in which capital is borrowed, misleads unthinking men into the opinion that the rate of interest depends on the quantity of money. No opinion can be more erroneous. As capital, consisting of commodities, using the term in its widest sense, and services, affords the means by which production is carried on, it is obvious that the price paid for its use must be governed by the supply of and demand for these means, and not on the supply of the medium by which they are transferred. An increase, therefore, in the quantity of available capital, the demand being unaltered, will lower the prevailing rate of interest. An increase in the quantity of money will raise prices, and can only have a transient effect on the rate of interest, during the short period which must elapse before its altered relation to commodities and services is ascertained, in other words, until it affects prices.*

* The "Economist," in an article published on the 8th November 1856, defined capital "as a certified right to a certain share of future production." The confusion of ideas involved in this definition will be apparent if we consider the case of a farmer who has a growing field of wheat but is without money to pay for the labour of reaping and threshing it. He has a certified share of future production in his coming crop of wheat, and thus, being a capitalist, according to the "Eco-

These are simple facts; but simple as they are, many care not to recognize them in the eager race for gain. There is a constant tendency, during times of prosperity, to embark in a larger amount of undertakings than the disposable capital of the country can support. Demands for credit increase, in consequence, when credit itself is declining from the insufficiency of the sources of supply for all the demands upon it; and bankruptcy and distress are the too frequent result.

On such occasions, the internal resources of bankers cannot be expanded to meet the demand. The deposit fund contracts, and the source of credit is dried up. Yet an opportune arrival of gold from abroad might effect a sudden change in this state of things. By reinforcing the reserves of bankers, it might restore confidence in their operations, relax the restrictions on credit, and arrest an impending fall of prices. What gold would effect by a solid expansion of the circulation, an increased issue of Bank of England notes might produce for a time, but with this important difference, that if the notes be issued on credit in excess of the amount which might be supplied by gold under like circumstances, the favourable reaction would be fleeting, and the relapse more calamitous. The history of commercial crises, which will hereafter be adverted to more particularly, abundantly confirms this conclusion; and, if it be sound, it follows that, when the quantity of coin and notes is undergoing diminution, the fund represented by book credits in general, must in the very nature of things be influenced by that contraction of the circulation, to this extent, at least, that at such times they can hardly be expanded so as to affect prices. Book credits with bankers are not, therefore, to be confounded in their general effects with bank notes.

nomist," he may obtain money by borrowing it from himself. In other words, the labourer may be fed with corn yet in the fields, and may be clothed with wool yet on the sheep's back.

These views may be further illustrated by a reference to the operations of the clearing house in London. By that simple and ingenious scheme, which has been brought to perfection since the admission of the joint stock banks to the Association in 1854, the whole of the drafts held by each bank upon others, and orders of all descriptions for transfers, are adjusted by mutual sets-off, until the actual payments to be made for the purpose of closing the accounts are reduced to comparatively small balances. All these bankers keep accounts with the Bank of England, where a special account is opened for the business of the clearing, upon which those bankers draw in whose favour the balance of the clearing may be. The whole of these vast transactions, amounting in the aggregate to several millions daily, are thus finally settled without the employment of a single bank note.

The economy of banking seems to be brought to perfection by this arrangement; and the amount of the circulation of coin and bank notes required for the great commerce of the metropolis is reduced within comparatively narrow limits; but the inference would be very erroneous that, because money is dispensed with to a great extent by these economizing expedients, its essential character is at all altered, or that it ceases to be the real regulator of prices.

The changes in the circulation which have resulted from the admission of the joint stock banks to the clearing house will throw much light on this question. It was to be expected that the effect of this measure would be shewn in a reduction of the circulation of notes of the higher denominations, by means of which large transactions requiring money payments are usually effected. Accordingly the accounts of the Bank of England exhibit a sensible diminution in the quantity of bank notes of this discription since 1853, when arrangements were first adopted by the private and the joint stock banks for making payments

to each other by drafts on the Bank of England, instead of by bank notes, followed in the succeeding year by the admission of the joint stock banks to the clearing. In 1853, the yearly average of Bank of England notes in the hands of the public was 22,633,000*l.*; in 1855 the average was reduced to 19,793,000*l.*; and the details of the different denominations of notes in circulation show that this reduction is wholly attributable to a diminution of notes for the higher amounts. For example, the notes in the hands of the public consisted

In 1853, of £5 to £10 notes	-		£10,699,000
„ 20 to 100	-	-	6,393,000
„ 200 to 1000		-	5,541,000
Total			£22,633,000

In 1855, of £5 to £10 notes		£10,628,000
„ 20 to 100	-	5,706,000
„ 200 to 1000	-	3,459,000
Total		£19,793,000

It thus appears that during these three years the average of notes of the smaller denominations, which are chiefly used by the public for current payments, remained much the same in amount. A diminution to the extent of 687,000*l.* is perceptible in those ranging from 20*l.* to 100*l.*, the use of which would be affected to some extent by the introduction of the new system; but the great change has occurred in the notes of a higher denomination, the reduction of which, during the period referred to, was no less than 2,082,000*l.*; the total reduction amounting to 2,769,000*l.* And it is clear that this great saving in the circulation is attributable solely to the economizing

arrangements adopted in London, since the average circulation of notes in the country underwent, during the three years in question, little change. *

Important considerations bearing on the general question may be gathered from a more detailed examination of the statistics of the circulation from which these figures are taken. It will be observed from the table in the Appendix that, from the time of the passing of the Bank Act of 1844 to 1853, the circulation of the various descriptions of notes bore a pretty uniform relation to each other. The variations in this respect are chiefly observable at times of great activity of trade, or of monetary difficulty, it being the general rule that the action upon bank notes of the higher denominations, whether in the direction of an increase or decrease in the circulation, precedes that upon notes representing smaller sums. The reason is obvious. The trade which is set in motion by large transactions, leads to the active employment of money of the description which passes most readily from hand to hand, and the increase of notes of smaller denomination is therefore the consequence, and not the forerunner of the extension of credit, which is indicated by the augmentation of those of large denomination. A contraction of the circulation on the other hand is first felt in the diminution of larger transactions. It will follow that among the most important liabilities which devolve upon a banker, is the contingency of demands for coin, or small notes, which will follow the extension of his book credits; and the extent of this demand, and the means which he may possess of meeting it will necessarily be a subject for anxious care.

This, then, is the sum of the whole matter. As prices

* The author is indebted for the information from which the foregoing statements are abstracted to Mr. Miller, of the Bank of England, to whose intelligence and exertions the perfection of the recent arrangements for the clearing is mainly attributable. Further details on the subject will be found in a tabular statement printed in an Appendix to this Tract.

must in the end be governed by the ability of the multitude of people to purchase commodities, so that ability must be derived from the quantity of money which is in daily circulation. The proportion which money bears to the trade carried on must still, therefore, be the measure of value, notwithstanding banking expedients for economizing its use. And although, with each extension of those expedients, the quantity of money in circulation, relatively to the amount of book transactions, will undergo modifications, the character of a banker's liability will remain the same.

Before dismissing this part of the subject, attention should be directed to one important feature of a highly-wrought system of credit. As it will necessarily be the care of a banker to maintain a reserve proportionate to his liabilities, an action on the deposit fund, leading to a diminution of the reserve, will affect in a multiplied degree the superstructure of credit. If, for example, the reserve be 1,000,000*l.* against 10,000,000*l.* of deposits, being in the proportion of one to ten, the withdrawal of 500,000*l* would alter the proportion to one to twenty, and, in order to restore the former condition, five millions of liabilities must be cancelled. Hence a diminution of only 1,000,000*l* in the stock of bullion in the Bank of England—the great reserve upon which the circulation of the country rests—may, in certain conditions of trade, operate to the curtailment of operations to an extent far exceeding the value of the treasure exported.

On the other hand, the growth of credit, or its reinstatement after periods of prostration, is comparatively slow and tentative. Trade cannot at once be extended to the limits which it may ultimately attain on an increased money basis. Hence the accumulation of bullion in the Bank will sometimes exceed the apparent demands for the use of money. The most remarkable example of this phenomenon is afforded in the state of the circulation in the

autumn of 1852, when the quantity of bullion in the Bank of England at one time exceeded the amount of notes with the public.

Bills of Exchange.

As Bills of Exchange are the favourite security for temporary investments, the amount of these instruments in circulation will afford the best test that can be obtained, in the absence of detailed returns, of the fluctuations in the employment of deposits. Mr. Newmarch has rendered, therefore, great service to monetary science by his investigations, communicated to the Statistical Society, which have led to reliable estimates of the amount of bills in use during a series of years. He has, however, formed some theoretical conclusions on the subject, which are open to question, and these have been freely adopted by Mr. Tooke.

Mr. Tooke places bank notes in the same category with bills of exchange. He at the same time contends, that there is generally a tendency to an increase in the amount of bills when the circulation of notes is undergoing contraction.

It might be supposed that the notion intended to be conveyed by these assertions is, that bills of exchange take the place of bank notes in the circulation when the latter are withdrawn: but the following passage from the paper by Mr. Newmarch on the subject of bills of exchange raises a doubt as to whether such is the meaning of these writers:—

"The extent," Mr. Newmarch observes, "to which bills of exchange can be discounted, at any given time, is governed by two principal causes: (1) by the total amount of ready capital in existence; and (2) by the extent of the demand for ready capital for other purposes, such as loans to Governments and landholders, the construction of railways, houses, and so on."

If, then, the use of bills of exchange be governed by the amount of available capital—an undeniable proposition

—and there be yet a tendency to an increase of their amount when bank notes are withdrawn, it would follow that the circulation of bank notes is not governed by the amount of available capital. Bank notes, therefore, and bills of exchange, though placed in the same category, are supposed to be governed by different laws. Both conclusions cannot be true; but it will be seen that, in fact, both are incorrect.

Leaving Mr. Tooke and Mr. Newmarch to solve these inconsistencies, we may proceed to the consideration of the question of the place which bills of exchange occupy in our monetary system; not doubting that with the aid of Mr. Newmarch's valuable statistics we may arrive at a sound conclusion.

Bills of exchange are securities for deferred payments; and although, like deposits, barter, &c., they may be so employed as to dispense in many cases with the use of money, they cannot be regarded as fulfilling all its conditions. Neither can prices be affected by their employment in the same way that they are affected by the issue of bank notes. Efforts may indeed be made to maintain the high price of particular commodities through speculative purchases by means of bills of exchange; but even in these cases the time must come when such transactions must be reduced to the money standard; and the general range of prices are beyond the reach of speculations of this character.

Under all circumstances, the value of bank notes, payable on demand, is governed by laws different from those which govern the value of credits for deferred payments. This point is illustrated by the effect of the practice, cited by Dr. Smith, which prevailed with banking companies in Scotland nearly a century ago, of inserting in their notes what was termed the optional clause, under which they were enabled to postpone payment for six months after presentation of the notes, on condition of

adding legal interest to the amount demanded. The obligation to pay interest did not prevent such notes from becoming greatly depreciated. Bills of exchange, which are, from their nature, of the character of securities for deferred payment, are subject to like depreciation. They do not represent, at the time that they are issued, the value of the money indicated on the face of them; their value depends on the quantity of money which may be available for trade at the time at which they are negotiated, on the anticipations entertained of the quantity of money which will be available when they become due, and on the reputed solvency of the persons whose names are upon them.

The conclusions aimed at by writers who confound bank notes with other securities for money, are by none of them clearly stated. They are satisfied with raising that degree of doubt and uncertainty which is favourable to speculative argument, and while they maintain in words the principle of a metallic standard, they seek to assign to bank notes a place in the circulation which would in truth obtain for them a character different from that which they possess as substitutes for coin. Hence, in their treatment of the subject, they studiously avoid all reference to the effect on the bank note itself of the provisions of the Bank Charter Act of 1844. They still treat the note as an instrument of credit, and refuse to give the attention due to the very important facts that, since the limitation upon the issues imposed by the Act of 1844, the Bank of England has no more to do with the creation of bank notes, and has no more command over them as a means of affording accommodation, or of discharging an obligation, than any other bank; and that every new note which is issued from the Bank of England is a certificate of value deposited and at any time reclaimable. Notes issued against bullion or a fixed amount of securities, and made by the State a legal tender for payments, possess all the attri-

butes of paper-money. If they be not paper-money, the term is without meaning.

The common sense of mankind sometimes goes astray; in this instance it leads to just conclusions. A man who has bank notes in his pocket calls them money; not so, if he has bills of exchange.

We are not, however, left to conjecture on this subject. Mr. Tooke, in reliance on the statistics of Mr. Newmarch, or rather on the reasoning which that gentleman has founded on his statistics, has reduced the question to a practical issue. The whole discussion resolves itself into the simple fact, whether or not the use of bills of exchange has increased, when the amount of coin and notes has been undergoing diminution; and it will be hard if, after the labour which has been bestowed on the investigation, we cannot arrive at a satisfactory result.

Mr. Fullarton, in a passage quoted by Mr. Tooke, thus commented upon an observation made by Mr. Norman on the subject:—

"I know indeed that it has been alleged that 'when the aggregate amount of coin and bank notes is undergoing diminution, an increase in the use of bills of exchange is, practically speaking, impossible.'" (*Mr. Norman's Letter to Charles Wood, Esq., M.P., p.* 42.)

"Now I believe this to be one of the many fallacies which have been invented *to prop up the rotten fabric of the Currency theory*. If my space permitted, and the occasion demanded, I am confident that I have the means of proving that there exists no such invariable connection, as has been generally assumed, between the expansions and contractions of the bill circulation." (*Regulation*, p. 47.)

Upon this passage Mr. Tooke makes the following comment:—

"The assumption implied in the statement here quoted from Mr. Norman, is an apt illustration of the exceedingly

unsatisfactory consequences which flow from discussing questions of currency from a purely abstract point of view; for few persons are better able than Mr. Norman to appreciate the testimony of facts on such a topic, or more willing to give to such testimony a candid attention.

"The truth really is, as affirmed by Mr. Fullarton, that there is no invariable connection between the variation of the bank note and the bill circulation, unless, indeed, it be a connection the precise reverse of that assumed by the currency party; for it has been shown conclusively by Mr. Newmarch, that, while the average total amount of inland bills of exchange in circulation at one time in Great Britain was 113,000,000 in the bad year of 1847, and 109,000,000 during the four bad years 1839-42, it was only 99,000,000 during the four prosperous and active years 1843-46. In other words, that at those periods, when banking accommodation and discounts —or, as the currency expression is, when 'bank notes'— were most difficult to be procured, bills of exchange were most numerous. The *rationale* of such a result is not very difficult, but into that part of the argument it is not material to enter at present."

There is a greater error than that of discussing questions of currency from a purely abstract point of view, and that is, endeavouring to support unsound theories by partial abstracts from statistical information. The figures furnished by Mr. Newmarch are reliable; but if, instead of forming an opinion upon an arbitrary average derived from grouped selections for series of years, the details supplied in his own tables had been studied, they would have been found to give results entirely confirmatory of Mr. Norman's view.

It may be observed that these denouncers of a "rotten theory" have not thought it necessary or convenient

to follow correctly the statement of Mr. Norman. That writer did not assert that there "is an invariable connection between the variation of the bank note and the bill circulation;" but that, when the aggregate amount of coin and bank notes is undergoing diminution, *an increase* in *the use* of bills of exchange, to an extent calculated to nullify the effects of this contraction, is, practically speaking, impossible. The sneer of Mr. Fullarton is supposed to be justified by the statistics of Mr. Newmarch; but the latter gentleman would probably have examined his figures with more care, before he committed himself to the opinion on which Mr. Tooke relies, if he had borne in mind the distinction drawn by himself between the creation and circulation of bills of exchange, and also his clear exposition of the principle on which he calculated the average amount of bills in circulation from Stamp-office returns, by a reference to the usance applicable to these securities. It is well known that in times of pressure advances are made for shorter terms than when the money-market is easy: speculators, when they have difficulty in meeting their liabilities, are also driven to the expedient of renewing their bills. The quantity created may thus show an increase from Stamp-office returns, while the quantity in use or circulation may be diminished. The character of bills in circulation will form a still more important element in arriving at a sound conclusion on the subject. It is the inability of traders to meet their engagements that creates mercantile distress; and the large amount of their bills in circulation in "a bad year," to use Mr. Tooke's term, will only show the excess of credit which had prevailed. What was the character of a large proportion of the bills in 1847? Let us hear what Mr. Samuel Gurney said on this subject in his evidence before the Commons' Committee of 1848:—"Experience has shown that a large proportion of these were of a very unsubstantial character." "A much larger per-

centage of the bills that fell due were unpaid than I ever knew before." "There were a great many renewals." (Qu. 1665—1667.) He had previously stated (qu. 1661) that the amount of commercial paper offered for discount at the date of his evidence, 25th February, 1848, was "very limited." From these facts, and from the conclusions derived from general reasoning, it might be conjectured that from the years 1839 and 1840, a period of great difficulty, there would be a progressive decrease in the quantity of bills of exchange; that they would be more largely employed from 1843, when, with an increasing circulation of bank notes, great activity in trade began to prevail; that when this activity assumed the character of excessive speculation, bills would obtain a more extended circulation, and that after the failures of 1847, they would undergo a sudden diminution. Let us now refer to the amount of bills in circulation in these years, as shown in Mr. Newmarch's tables:—

Total amount of Inland Bills in circulation at one time in Great Britain.

1839	- - -	£113,119,000
1840	- - -	116,319,000
1841	- - -	107,903,000
1842	- - -	92,751,000
1843	- - -	87,659,000
1844	- - -	91,004,000
1845	- - -	106,030,000
1846	- - -	112,532,000
1847	- - -	113,161,000

In 1848, the amount of the stamp-duty on inland bills of exchange was 452,762*l.* (against 525,854*l.* in 1847), which, on the data for calculating the circulation adopted by Mr. Newmarch, would give 97,293,000*l.* as the amount of inland bills in circulation in 1848, being a decrease

of more than one-sixth on the amount of the preceeding year.

It thus appears that there is no ground for concluding, from the very small increase of bill stamps in 1847 over those of the preceding year, that any increase occurred in the circulation of those instruments in 1847; but that, on the other hand, a large decrease did occur in 1848, when, be it remarked, the active circulation of notes in the United Kingdom was undergoing a rapid diminution, from 37,941,158*l.* on the 27th March, 1847, to 32,872,750*l.* on the 25th March, 1848.

The result affords corroboration of the accuracy of Mr. Newmarch's calculations, and shows, at the same time, the fallacy of the reasoning which in this instance he has founded upon them.

The essential character of bank notes

Having disposed of the questions regarding the monetary functions performed through the means of deposits and bills of exchange, we may now consider the essential character of bank notes.

Bank notes are only instruments of credit in the sense of their possessing no intrinsic value, passing as they do from hand to hand on the credit of those by whom they are issued. As long as they thus pass current, they perform all the functions of money within the range of their circulation,—attributes not united in any other form of paper credit. The principle on which they circulate is thus stated in Smith's "Wealth of Nations:"

"A paper money, consisting of bank notes, issued by people of undoubted credit, payable on demand, without any condition, and, in fact, always readily paid as soon as presented, is, in every respect, equal in value to gold and silver money, since gold and silver money can at any time be had for it. Whatever is bought or sold for such paper must necessarily be bought and sold as cheap as it could have been for gold and silver."

It is clear that the two conditions of undoubted credit and perfect convertibility are necessary to ensure to bank notes the value claimed for them in this passage. It is only when those conditions are absolutely fulfilled that these instruments can possess the attributes of paper money, and that identity in value between them and the coin which they represent can exist.

No sound opinions can be formed on the subject of the part which is performed by the various aids to the circulation, unless a clear classification be maintained, and the essential character of money be kept steadily in view. The possession of intrinsic value is the most important attribute of coin as without that quality it cannot fulfil its functions as a measure of value; and it follows that whatever may be taken as its representative should at all times command that value. In this respect, the most complete form of paper money would be a note given for bullion deposited, and reclaimable on demand,—such as would exist at Hamburgh, if instead of credits being raised at the deposit bank in the name of the depositor of bullion, notes payable on demand were issued for the value of each deposit. There can be no question that such notes would be perfectly identical with coin. They would fulfil just the same functions, and represent the same value. The only difference would consist in their superior convenience, in the economy arising from the saving of the wear of coin, and in the saving of labour and time, which would otherwise be consumed in obtaining the coinage of the bullion. If such a practice had from the first existed in the case of the Bank of England, it might be conceived that the Government, under pressure of political difficulties, might at some time have appropriated a portion of the treasure lying idle at the Bank; and if the abstraction were made, without the cognizance of the public, for the purpose of a foreign payment, it would not have had any apparent influence on the circulation of the country: the notes would

still have circulated as certificates of value, and if a sufficient reserve of bullion had been left, gold would still have been obtained for them, on demand, as freely as before. The result in the supposed case, is precisely the same as that which arises in the case of notes issued by the Bank of England, under the restrictions imposed by the Act of 1844. The term paper-money could hardly be withheld by the most fastidious stipulator for intrinsic value from notes issued under the supposed system ; and if it be conceded in that case, it cannot with consistency be withheld in the other.

But, although in point of security, the Bank of England note has been greatly improved by the restrictions of the Act of 1844, it cannot be said that its functions as a medium of exchange are at all altered by that Act. It previously, as now, passed from hand to hand as money, and discharged all descriptions of debts. Neither can it be denied that the promissory notes of other banks possess the same attributes within the limits of their circulation. The degree of security is different, and the derangement of the circulation arising from over-issue has yet to be considered; but so long as the credit of the issuer is unquestioned, bank notes in all cases fulfil within their range the same functions, and those functions are the functions of money.

The abuse of the power of issue constitutes, therefore, a subject of general concern; and the rash notions which would confound this power with the exercise of credit between bankers and their customers, cannot be entertained with prudence or consistency.

So far from the fact of the extensive use of credit instead of money affording a reason for leaving bankers unfettered in the power of issuing notes upon credit, the great extent to which the use of money has been already economized would lead to an opposite conclusion. The effects upon trade of the increase of late years in banking

accommodation may be conjectured from the following facts: The circulation of the Bank of England at the time of the final resumption of cash payments was nearly double the amount at which it stood at the time of the suspension of cash payments in 1797. In the interval of those years the trade of the country had so increased as to give employment for this great addition to the medium of exchange. On the 31st of August, 1821, the circulation of notes of the Bank of England for 5*l.* and upwards (including post bills) amounted to 17,747,000*l.* On the 31st of August, 1827, it had increased to 22,267,000*l.*, owing to exceptional causes. Since that date, until 1852, the amount of Bank of England notes outside the Bank generally ranged between 18,000,000*l.* and 20,000,000*l.*, except during the depressed period of 1840 and 1841. The highest amount which it has ever attained was 25,297,000*l.* on the 16th of July, 1853, arising from the large imports of gold from Australia, which threaten, if they have not realized, some depreciation of that metal. The average amount in the year 1855 was 19,795,000*l.* Let us contrast this condition of the circulation with the progress of the nation during the period referred to. From the Income Tax Returns it appears that, since the year 1814, the taxable income of the country has doubled. The population of England by the census of 1821 was 11,261,437; by the census of 1851 it was 16,826,492 being an increase of more than 50 per cent. over the numbers of the former year. The declared value of British and Irish produce exported in 1821 was 36,659,630*l.*, in 1855 it was 95,688,085*l.* The tonnage of British and foreign ships entered into ports of the United Kingdom amounted in 1821 to 1,995,530; in 1855 to 8,951,239. The tonnage of such vessels cleared outwards amounted in 1821 to 1,872,430; in 1855 to 9,538,231. These figures indicate an enormous increase in the wealth of the country, and yet, owing to the

facilities afforded by bankers and others in the transfer of credit and capital, this extended trade is carried on without any addition to the notes in circulation.*

Two reflections suggest themselves from the foregoing remarks, namely, first, the extreme importance of maintaining the integrity of the money basis, on which so vast a superstructure of credit rests; and, secondly, the comparative insignificance, in regard to the interests of the public at large, of any further saving of expense in economizing the use of the precious metals, which would arise from an additional issue of paper-money on the credit of securities.

* The great increase of gold in circulation arising from the withdrawal of 1*l.* notes, does not affect the question of the present circulation of the Bank of England: the notes formerly issued for sums under 5*l.* have been excluded from the comparison of the circulation of 1821 and the present time.

SECTION IV.

EXAMINATION OF THE QUESTION WHETHER THE LEGAL CONVERTIBILITY OF BANK NOTES WILL PREVENT EXCESSIVE ISSUES AND DEPRECIATION.

THAT the convertibility of bank notes is necessary to insure the maintenance of their value in exchange, and to correct eventually excess in the circulation, is a proposition that will not admit of dispute; but experience has proved that the obligation of payment on demand has not operated as a sufficient check upon banks to prevent over-issue. The conduct in this respect, both of the Bank of England and of Scotch banks in past times, and its consequences, have been clearly demonstrated by Adam Smith. The disasters arising from the reckless proceedings of English banks in 1825, the difficulties in which the Bank of England has been placed on various occasions, the frequent and extensive failures of banks in the United States up to very recent times, and similar results in our colonies and on the continent of Europe, have all tended to prove that the power of uncontrolled issue is liable to great abuse, and may lead to results disastrous alike to those who exercise it and to the public at large, who are involved in the consequences. Yet the opponents of the Bank Act of 1844 reject the lessons of experience, and deny the possibility of the over-issue and depreciation of notes which are payable on demand.

Mr. Fullarton thus expresses himself on this subject, in a passage quoted by Mr. Tooke :—

"As a general principle I am free to admit that the increase or decrease of a circulation of bank notes, from whatever cause it may proceed, ought to correspond with the increase or decrease which the currency of metallic

coin would exhibit under the same circumstance. But I go further than this; I contend that there not only ought to be such correspondence, but that there always is; that whenever the convertibility of the paper is perfect, and secured from all delay and impediment, the coin of full standard weight and fineness, and the traffic in the metal, whether coined or uncoined, absolutely free and unrestricted, then the bank issues, if left to themselves, must necessarily fluctuate in conformity with the principles which govern the supply of the standard metal; and it is only from the intervention of some such arbitrary and empirical system of restraint as is now projected, that this uniformity runs any risk of being disturbed."

It is to be regretted that the view stated in this passage, which Mr. Tooke characterises as being distinguished by "wonderful clearness and vigour," was not further illustrated by showing in what manner a restriction which prevents the issue of additional notes except on the deposit of the standard metal, could possibly have the effect of preventing the bank issues from fluctuating in conformity with the principles which govern the supply of that metal; and what objection exists to the Act of 1844, if the action which it necessitates be not only desirable but unavoidable.

Mr. Wilson, however, who adopts the same view, confines his argument, with greater plausibility, to the question of the depreciation of the note. He observes, that "it is difficult to conceive any state of circumstances that would induce the public to retain in their possession a lower representative of value, when the mere trouble of stepping to a bank and presenting it for payment would instantly put them in possession of a higher and more valuable instrument of exchange."*

* Article in the "Economist," April 5, 1845; page 53 of the published volume.

And he asks—

"What in reality does excess of issue and consequent depreciation mean? If it means anything, it is that the paper in circulation will not command the full quantity of coin which it represents, or exchange for the same quantity of other commodities as coin would."*

Well may Mr. Tooke observe upon "the exceedingly unsatisfactory consequences which flow from discussing questions of currency from a purely abstract point of view," when so able an expounder of political economy as Mr. Wilson is led, from adherence to a favourite but untenable theory, to misstate the question in dispute, and answer it by a reference to a supposed case which could not occur.

It is evident that, so long as the credit of a bank is maintained, its notes while in circulation will pass current at the same value, and purchase the same quantity of commodities as the coin which they represent. Over-issue, or, which is the same thing in effect, neglect to contract issues, when the state of the foreign exchanges creates a demand for specie for exportation, leads to the consequence, not of depreciating notes relatively to coin in internal circulation, but of depreciating the whole circulation, combined of coins and notes, as compared with the money of other countries. Notes in such a case will not be presented for payment in order to obtain coin with which to purchase a larger quantity of commodities at home, but with the view of obtaining specie for exportation; and if bankers omit to counteract this demand by reducing their issues and strengthening their reserves, further depreciation and other inevitable consequences of imprudent extension of credit must ensue.

There is no example of any hesitation on the part of the public to receive and pay bank notes for the value

* Article in the "Economist," April 5, 1845; page 53 of the published volume.

which they represent, so long as no doubt has been raised regarding the ability and disposition of the issuer to fulfil the obligation of immediate payment on demand. Depreciation of notes relatively to coin has only arisen from obstructions opposed to the fulfilment of this condition. Such was the effect of the optional clause formerly inserted in bank notes in Scotland, which has been already adverted to: such, also, was the effect of difficulties at one time raised by banks in the United States in order to discourage the presentation of notes for payment; and such is the general consequence of a suspension of specie payments. In all these cases, so long as the ultimate solvency of the issuing body is unquestioned, bank notes may continue to circulate even after their depreciation relatively to coin has been admitted. But a different state of things is contemplated by the opponents of the Act of 1844. They suppose a condition of the circulation in which bank notes pass from hand to hand on faith of their immediate convertibility on demand; and contend that, under such circumstances, no depreciation of the circulation can occur.

The fallacy of this opinion will be apparent if we consider the nature of depreciation of the circulation. It is tantamount to a rise in the money price of commodities, occasioned by a relative increase of the circulating medium. High prices, however, may proceed from many causes; and the actual cause in operation may escape the notice of the public. When they arise from undue excitement in trade, they are accompanied by an unusual demand for labour and services. With dearness of living there comes the compensation of remunerative employment; and many are thus interested in the race of competition. While money is forthcoming in the shape of bank notes, no motive for comparison arises. The faith in the solvency of the banks may remain unquestioned until suspension of payments is announced; and until

then the fact of depreciation may be unperceived by the community at large.

Speculations leading to a rise in prices generally originate in an abuse of credit. The increased circulation of bank notes, when the issue is unrestricted, follows as a consequence, in order to support the trade thus set in motion. Mr. Wilson, and other writers holding the same opinions, do not acknowledge this connection of cause and effect: they contend that the grant of credits is the act of bankers; but that the circulation depends on the action of the public, and is beyond the control of the issuing body. The distinction sought to be established is an illusion. The action of the public on a bank can only arise from credits previously raised. The public draw upon a voluntary source of supply so long as the banker has the power of extending his credit circulation by an unlimited issue. The assumed action of the public operates, on the contrary, as a powerful check on the abuse of credit when a restriction on the circulation is imposed by law; and when, as a natural consequence of such restriction, undue facilities for the extension of trade lead inevitably and quickly to demands upon those who afford them for hard and substantial money.

The history of banking in the United States may be referred to with advantage in illustration of this point. Reliable information of the condition of the joint-stock banks of that country at different periods is available, which is not generally afforded in the case of the private and joint-stock banks of Great Britain; and we may trace, therefore, with greater accuracy, the progress of their transactions. In the early part of the year 1835, in which year enormous additions to the issues of the United States banks commenced, the aggregate amount of their loans and discounts was $365,163,834; and the average amount of notes issued by them was $103,692,495. By the commencement of 1837, the loans and discounts had

increased to $525,115,702, and the circulation of notes to $149,185,890. These figures abundantly prove the connection which exists between the circulation of notes and the book transactions of bankers; for while the credits were increased by the addition of two-fifths to the amount at which they stood at the commencement of the period, the issues of bank notes were extended in a still larger proportion. And it cannot be pretended that these issues involved no depreciation of the circulation. The fever of speculation and the consequent rise in prices which existed during the period are notorious; and the stoppage of the banks which followed shows, as far as facts can show, that in the enormous addition to their issues, those banks far outstripped the limits within which they would have been confined if they had attempted to regulate the circulation by the laws which regulate the currency of metallic coin. The excess of their issues led in 1837 to a general suspension of cash payments, and the failure of many banks. Although cash payments were resumed in the following year by the banks which remained, a great part of them, including the Bank of the United States, again suspended payments in 1839. That institution, with many others, proved in the end to be insolvent. Between 1830 and 1840, no less than 150 banks, having an aggregate capital of $45,000,000, became entirely insolvent. Between February 1841 and September 1842, 161 additional failures of banks, with an aggregate capital of $132,362,339, took place.* The collapse and long stagnation of the trade of the country which ensued are now matters of history; and the lessons of experience will be lost to us if, in the face of this tremendous example of the consequences of vesting in banks the uncontrolled privilege of issue, we give credence to the dangerous hypothesis of modern economists, that this power is innocuous.

* These details are extracted from Mr. M'Culloch's "Commercial Dictionary."

The United States themselves have profited to some extent by this severe lesson. Banks of Issue are now required to lodge public securities for the amount of their issues: and although this precaution does not secure the fulfilment of the cardinal requirement, that the paper circulation should conform to the rules which would govern a metallic circulation and although it has not prevented the failure of banks in some States, the present condition of the banks of New York and the general conduct of the banking business of the Union affords a favourable contrast to the reckless course exhibited when the issues were unrestricted.

Divested of speculative disquisition, the discussion resolves itself into the practical questions, whether it is expedient to permit banks to issue paper money under circumstances in which they could not employ coin; and, if that question be answered in the negative, what is the nature of the restrictions required for the security of the public.

In order to prove that the power of issue has been abused, it is not necessary to show that it has been the originating cause of excitement and over-trading. Excessive speculation generally arises from an abundance of floating capital seeking investment. In such case it is not until credit has been incautiously extended, and prices, in consequence, have begun to rise, that the contagion has spread to the issuing bodies; and the evil of over-issue has been chiefly shown in the neglect to take timely warning, and contract the circulation on the first evidence of redundancy. The effect of an excessive circulation in aggravating the consequences of previous derangement of prices, has been ably expounded in the following passage from the evidence given by Lord Overstone, before the Select Committee on Joint-Stock Banks, in 1840:—

"The excitement (to use one word to express a variety of phenomena) which took place in the years 1834 and

1835, I do not attribute to the state of the circulation as the originating cause. Excitement in commercial and trading affairs arises from a great variety of causes. But when that excitement has taken place, it necessarily tends to produce a rise of prices; that rise of prices produces an increased tendency to imports and a diminished tendency to exports, consequently a drain of bullion ensues; and if the circulation be properly managed, a contraction of the aggregate paper circulation will take place in correspondence with that decrease of bullion. That contraction of the aggregate paper circulation will necessarily tend to check and control the excitement and the rise of prices. But if that contraction of the aggregate paper circulation does not take place, then the excitement and rise of prices will probably continue; and the continuance of the excitement and of the rise of prices is then, in my judgment, justly attributable to mismanagement of the circulation. The view, therefore, that I take of those two periods, and of the time that intervened, is this; that the excitement and rise of prices was suffered to go to a greater extent than they would otherwise have reached, because the aggregate paper circulation was not contracted simultaneously with the drain of bullion. I therefore attribute the continuance of the rise of prices, not the origin of that rise, to the mismanagement of the circulation." (Qu. 3,580.)

Mr. Tooke, who once coincided in these views, pointed out very forcibly in his evidence before the Committee of 1832, the demand which arises for an increased issue of notes at times when general considerations of the state of the exchanges ought to induce a contraction of the circulation.

"The demand, he observes, "for accommodation in the way of discount or loan by individuals, is very often, if not generally, in exactly an inverse ratio to the demands of the circulation, so that at the time when there is the greatest inducement among the customers of country banks, or of the Bank of England, to borrow, is very often

precisely that period at which it is most essential to contract the circulation; therefore there is very often an excess of issue through the medium of private credit, which would not occur if the issues were regulated on the principle of substitution of paper for what otherwise would have been the circulation of gold." (Qu. 3,960.)

It is surprising that a writer who was at one time so capable of forming a clear judgment upon causes and effects, should have fallen into the error of Mr. Fullarton, in adopting the opinion that legal convertibility alone must ensure conformity of the circulation of bank notes with the ebbs and flows of the metallic basis. The most cursory examination of figures showing the fluctuations of the circulation and bullion, at times of monetary derangement before the Act of 1844, must at once dispel this illusion.

Take for example the published returns relating to the Bank of England in the years 1824 and 1825:—

	Circulation of Bank notes of £5 and upwards, and Post-bills.	Bullion.
	£	£
February 28, 1824	19,250,860	13,810,060
August 31, „	19,688,980	11,787,430
February 28, 1825	20,337,030	8,779,100
August 31, „	19,002,500	3,634,320

It is clear, from these figures, that the issue of Bank of England notes was increased up to the first part of the year 1825, in the face of a drain of bullion; and that when, by the end of August in that year, the amount of notes had been again reduced below the circulation of the early part of 1824, more than 10,000,000*l.* of bullion had been, in the meantime, withdrawn from the Bank.

On the 28th of February, 1824, the amount of notes issued on credit by the Bank, that is, of notes uncovered by bullion held in reserve, was 5,440,800*l.* On the 31st of August, 1825, this issue on credit had risen to 15,368,180*l.*, to which must be added the increased issue of country notes, estimated at 4,000,000*l.*, making a total increase of 19,368,180*l.*, in the credit circulation of England. The most ingenious sophistry could not give a colour to the notion that this increase was in conformity with the laws which would govern the supply of a purely metallic currency.

Again, in the month of September, 1833, the average amount of bullion in the Bank of England was 10,844,250*l.*, and the circulation of notes in the United Kingdom was 36,035,244*l.* By the month of September following, the bullion was reduced to 6,991,600*l.*, and the circulation increased to 36,727,131*l.* It would be waste of time to follow out these illustrations further.

SECTION V.

THEORIES OF MR. TOOKE AND THE "ECONOMIST," REGARDING PRICES AND THE CIRCULATION, EXAMINED.

Tooke's ry that Circulating ium is the equence of es.

IT has become the fashion among writers of this class to ridicule the system established in 1844 as the "Currency theory:" but if the term "theory" be properly applicable to a measure which, whether right or wrong, is indisputably of a very practical character, its opponents have not been found wanting in theories to disprove its efficacy. Among the most remarkable of these theories is the following dictum, the fruitful parent of other fallacies, first propounded by Mr. Tooke, in a "series of conclusions" stated in a work published by him in 1844, and reannounced in his recent pamphlet:—

"That the prices of commodities do not depend upon the quantity of money indicated by the amount of bank notes, nor upon the amount of the whole of the circulating medium, but that, on the contrary, the amount of the circulating medium is the consequence of prices."

If it were meant by the concluding phrase of this paragraph, that prices are the means by which the distribution of the precious metals throughout the world is regulated, the proposition would be a mere truism stated in ambiguous language.

But in order to trace the writer's meaning, it is necessary to disregard the transition from the term "bank notes" to that of "circulating medium," and to define the

passage by a reference to the sense in which he uses the latter phrase.

Now, according to Mr. Tooke, circulating medium consists of bank notes, bank credits and bills of exchange;* in short, all forms of credit, combined with coin. In this sense the proposition supposes that, when prices are high, credit must be maintained to support them, and we become at once involved in that labyrinth of ill-defined value, which found advocates before the Bullion Committee of 1810, but into which none but a zealot for non-convertibility would now willingly enter.

If, however, the passage imply that prices regulate the supply of money or of currency representing money, and if we are to accept it in some other sense than that of stating the means by which the precious metals are distributed, Mr. Tooke's dictum involves a transparent fallacy. Political economy is not a science of one country, but treats of laws which govern the commerce of the world. Activity in trade has a tendency to raise prices, and if it be true that the quantity of current money is the consequence of prices, it would follow that from whatever causes activity in trade and consequent demand for money may arise, including in such causes undue speculation, money will be obtained to supply the required circulating medium. But activity in trade, leading to a rise in prices, may prevail in every country in succession; and the absurd conclusion would ensue that all countries collectively may require and obtain more money than all the world contains. Such are the results to which men are led by speculations, formed in disregard of the broad principles which govern value and the distribution of the precious metals, as demonstrated by the reasoning of Dr. Adam Smith, Mr. Ricardo, and other eminent economists.

Yet Mr. Tooke's dictum has found an advocate in Mr.

* See his Pamphlet, page 20.

Wilson, and from the weight justly due to the opinions of that writer, it might be supposed that the hypothesis has been misunderstood. Let us therefore examine it further, by the light afforded by the "Economist."

Colonel Torrens, in a passage distinguished no less by keen wit than sound perception, had thus commented upon Mr. Tooke's proposition:—

"The logical accuracy of this conclusion may be tested by affirming the analogous proposition, that the prices of commodities in Europe, after the discovery of the mines of South America, did not depend upon the quantity of money, indicated by the amount of coin, nor by the amount of the whole of the supply of gold and silver; but that, on the contrary, the mines of South America, and the increased amount of gold and silver obtained therefrom, were the consequence of the subsequent rise of prices."

Upon this passage Mr. Wilson made the following rejoinder:—

"That this ingenious and accomplished economist should have stated these as two '*analogous propositions*,' is the most striking evidence with which we have yet met of the utter confusion which prevails in men's minds of the real nature of currency and capital, of coin as a circulating medium, and of the precious metals as a commodity of commerce."*

He proceeds to argue that, "in the case of an ordinary influx of gold into this country caused by a favourable state of the exchanges, the general quantity of gold is not changed, nor its relation in value to other commodities; a new distribution is all that takes place;" that "when merchants have recourse to bullion to bring home their capital from those countries where it is not produced," the fact affords evidence that other commodities cannot be

* "Economist," April 19, 1845; page 85 of the published volume.

imported but at a loss; that "this neither infers a power for an increased private expenditure, nor an inducement for a repetition of purchases for shipment;" and that "hence we find that in practice neither circulation nor prices increase under such circumstances, but both diminish."

Mr. Wilson illustrates this argument by a reference to the period from the beginning of 1841 to 1843, when we had an uninterrupted favourable exchange: during all that time, he states that the bullion rapidly increased from 3,965,000*l.* to upwards of 11,000,000*l.*, that every means were used, which properly could be used, to increase the circulation, and yet that it fell during that time from 35,660,000*l.* to 34,049,000*l.*

In correction of this statement, it may be observed that the increase of bullion referred to amounted to little more than the reinstatement of the reserve to the amount at which it stood in the first half of the year 1838; that so far from being rapid, that increase was gradual, and was occasioned by the steady recovery from the extreme depression of 1839. The bullion which passed into the reserve of the Bank became by that fact a part of the money of the country. Bankers, no doubt, tried to employ it; but the Bank acted with great caution, in consequence of the large imports of corn which took place during the whole period: the evidence of this caution is afforded by the fact that the minimum rate of discount was maintained at 5 per cent., until April 1842, when the stock of bullion having risen to 6,590,000*l.*, the rate was reduced to 4 per cent.

But in truth this influx of bullion was but the symptom of that returning prosperity which, commencing in 1843, led to the speculative period of 1845 and 1846. The bullion increased during this latter period, and with it the employment of money. At what time, then, did it alter its character of "a commodity of commerce," which, ac-

cording to Mr. Wilson's theory, it at first bore, and in what manner can the alteration be reconciled with that theory?

Still, apart from the theory on which they are founded, Mr. Wilson's observations merit attention. No one, who has studied the statistics of the circulation, can doubt that, under our system of credit, the imports or exports of gold, though influencing trade in the end, have not always an immediate effect on prices corresponding with the variations in the circulating medium.

Prices may remain, under certain conditions of trade, at a comparatively low level for a considerable time after favourable exchanges have been established and an influx of bullion has set in, and they may remain unaltered, under certain conditions of trade, for some time after an efflux of bullion and a contraction of the circulation. But the converse of these effects cannot under any circumstances be true. High prices cannot naturally command abundant circulation.

An example of the first effect is afforded by the very slow action on the employment of Bank of England notes, from the large importation of gold from Australia previously to 1852, which, according to Mr. Wilson's theory, the general quantity of gold having been changed by this additional supply, ought to have had an immediate influence on prices.

An example of the second effect is afforded by Mr. Tooke in his history of prices of the years 1838 and 1839, upon which he makes the following judicious comment:—

"Although the prices of commodities form the medium through which the tendency to a level in the distribution of the precious metals in the commercial world operates in the long run, there are disturbing causes which may, during very considerable intervals, act powerfully upon the exchanges, and induce, in a convertible state of the currency, a strong tendency to an efflux of the precious

metals, to counteract which extraordinary efforts may be requisite on the part of the regulator of the currency, which, in this country, is the Bank of England, while during the whole time there may be no intermediate derangement of the ordinary level of the prices of commodities."*

The only exception that can be taken to this passage is, that it contains a direct contradiction to the hypothesis under consideration. Sound maxims occasionally gleam through the cloud of opinions which pervades the works of Mr. Tooke. It would be absurd to underrate them because the author does not always maintain consistency. The reasonable course to follow in such a case is, to adhere to those opinions which he supports by cogent argument or reference to facts, and to reject the rest as the whims of a too fertile mind.

Further opinions of Wilson on same subje[ct]

The articles in the "Economist" from the pen of Mr. Wilson on the subject of the influence of prices on the circulation, are not confined to abstract reasoning in support of Mr. Tooke's theory, but take up the question on independent grounds, and reduce it to the test of practical results.

In the article of the 12th April, 1845, already referred to, it is contended that "an expansion or contraction of the currency is AN EFFECT and not A CAUSE;" and that "in all such changes the banker is a PASSIVE AGENT, acted upon by the circumstances which determine the amount of currency required, and not an ACTIVE AGENT, acting upon the amount of the currency." Mr. Wilson supposes that "if any attempt be made to curtail the currency by forcibly withholding bank notes from circulation, it will only oblige the public to withdraw from their deposits a larger quantity of coin." In support of this view, he refers

* Tooke's "History of Prices," vol. iii, p. 70.

to the unprecedented import of grain in 1839, which led to a great export of bullion, and shows that the efforts of the Bank of England to contract the circulation, when this drain commenced, were thwarted by the action of the country banks, which filled up the circulation by the issue of their notes, as rapidly as those of the Bank of England were withdrawn. So far from blaming the country banks for this proceeding, he contends that had they not increased their issues, "the bullion of the bank would have suffered a reduction during that period, to fill with coin the vacuum created in the requisite amount of currency by the withdrawal of bank notes. He states that "at this period of the drain, the Bank, conceiving that their plans for correcting the exchanges were frustrated by the expansion of the country circulation, took severe measures to check it," by refusing "to discount any paper having the endorsement of a joint stock bank of issue," and "that this act was accordingly succeeded by a sudden and violent attempt at contraction by the country banks."

The supposed consequences of these proceedings are represented in the following remarkable passages:—

"During the period, the drain of bullion was more severe than at any time before or after. On the 1st of June, the bullion in the Bank was 5,119,000*l.*, and in September it had sunk to 2,816,000*l.*, notwithstanding the loan from the Bank of France of 2,500,000*l.*; leaving which out of the question, we agree with Mr. Loyd that he would be justified in saying that 'the bullion of the Bank would have been completely exhausted.' But we think there is every reason to believe that the contraction thus forced on the country banks tended, during those three months, to aggravate the drain of foreign bullion, by withdrawing from the Bank the

coin required to sustain the requisite amount of currency."

"We think," the writer adds, "that it cannot be denied, that while bankers may forcibly contract that part of the circulation which consists of bank notes, they cannot prevent the whole amount being preserved by the withdrawal of deposits, and the substitution of coin for notes. We readily, however, admit that after the high price of corn, and the adverse exchange, had lasted sufficiently long to reduce the consumption of other commodities, to lessen the demand for manufactures, the amount of employment, and the sum required for the payment of wages, and consequently that applicable to the daily expenditure, the circulation would then of its own accord become contracted both of coin and notes. This contraction follows, however, as the EFFECT of these combined circumstances, and not as the result of any action on the part of the Bank."

The statement on which this extraordinary theory is founded is loose and inaccurate; but, before investigating the alleged facts and their consequences, it is desirable to examine the argument in support of which they are adduced. It is given in the very words of the writer, to prevent the possibility of misapprehension, and resolves itself into the following propositions:—

(1.) That bankers enjoying the privilege of issue, but subject to the legal obligation of paying their notes on demand, have the power of contracting the circulation of their notes, but that, if such contraction be attempted at an early period of a foreign drain of bullion, arising from an unfavourable state of the exchanges, it would only lead to the substitution of coin for notes.

(2.) That in such a case the coin alleged to be required will be obtained by the withdrawal of deposits.

(3.) And that the ultimate diminution of the active

circulation will be the effect, and not the cause, of contracted trade.

Let us examine these propositions seriatim :—

(1.) The admission that bankers have the power of reducing their circulation of notes is important. On this point Mr. Wilson is agreed with Mr. Ricardo, who, writing at a time when the suspension of cash payments was in force, observed as an undeniable fact, "that the Bank have the power of reducing the circulation within the very narrowest limits." This statement must, however, be taken subject to two qualifications, namely, first, that the limit within which the circulation can be reduced is that which would be the amount, under similar conditions of trade, of a purely metallic currency; and secondly, that the first effect of a contraction of the issue of notes may be to induce, under certain circumstances, a withdrawal of deposits and an apparent reaction for a short time upon the circulation.

In the first case, the contraction of the circulation below the natural limit would affect the exchanges and lead to an importation of bullion: in the second case, the action upon deposits by traders thrown on their ultimate resources by the failure of their expectations of extended credit, and, in the case of the Bank of England, by the requirements of other banks in order to strengthen their reserves against anticipated pressure, may occasion a demand for notes or coin at a time when the active circulation of the country is, in fact, in progress of diminution. Some attempt may also be made at the commencement of an adverse exchange to keep up prices by obtaining notes through an action on the deposits; but this would be checked by a sale of securities, and there is a minimum below which deposits could not be reduced. These are not, however, the contingencies within Mr. Wilson's contemplation. He does not refer to a temporary and excep-

tional action on deposits in consequence of pressure arising from the diminution of floating capital, but assumes an undeviating law that, in spite of any precautionary proceedings on the part of the Bank, the circulation must be maintained, under the influence of an adverse exchange, at the level of previous prices. He supposes, in apparent forgetfulness of the theory, for which he had contended in a former article, of the conformity of a mixed currency with the variations of a metallic currency; that there is a countervailing action between notes and coin; and that at a time when an adverse exchange is causing an export of bullion, any attempt to make the circulation of notes conform to the diminution of gold would only lead to an increased demand of gold for internal circulation. He is of opinion that high prices require abundant circulation; but he will not deny that high prices lead to an adverse exchange. Such a condition of the exchange indicates a depreciation of our currency, and leads to the export of gold. But according to Mr. Wilson's view, gold is, at the same time, retained for the purposes of internal trade because prices are high, and because, consequently, the currency is depreciated. One cause produces, in his opinion, simultaneously two opposite effects.

(2.) The means by which the supposed effect is to be produced are no less remarkable than the supposition itself. It is contended that while the Bank has unlimited power over the use of its notes, it has no power to contract the circulation when it consists of coin and notes combined, or of notes payable on demand and based on a reserve of specie. It would follow from this hypothesis that during the suspension of cash payments the Bank was able to prevent an excess of issue; but that its power in this respect ceased with the reimposition of the obligation to pay its notes on demand; that it then became spell-bound by a law never before contemplated by economists, and was subjected to the necessity of maintaining the circula-

tion in the face of a diminution of its reserve, owing to a foreign drain, even to the verge of bankruptcy.

The power which is supposed to produce these results is represented to be vested in the depositors. If the Bank of England contracts the use of its notes, the holders of deposits will, it is conjectured, rush in and obtain coin to supply the place of notes withdrawn from circulation. This allegation supposes that those who have lodged money, or the value of money, with the Bank, are identical with the class who require the use of it, or, in other words, that those who have money and those who wish to borrow it are the same persons; that this hybrid class consists only of depositors with the Bank of England, where the great reserve of gold to be thus acted upon is maintained, since it is said that the diminution of country bank notes will be counteracted, not by the action of depositors on those banks, but by the withdrawal of deposits in the shape of coin from the Bank of England; and, finally, that the Bank of England is debarred by its peculiar position from taking those precautions, in the management of the deposits entrusted to it, upon which its safety and well-being as a bank depend, and which are the very essence of the institution of banking. Deposits are usually withdrawn to a certain extent during a drain of gold, because the rate of interest rises, and it becomes profitable to employ them. They cannot, however, be diminished below a certain point, fixed by the habits of trade as respects bankers and their customers. Their is no difference in principle between the deposits of the Bank of England and those of other bankers: both are influenced by the same laws. But it is unnecessary to pursue further these speculations on an improbable, if not impossible, event; for there is one obvious consideration which puts an end at once to the whole assumption, and which it is surprising that a writer of so much discernment as Mr. Wilson should have overlooked. Bank of England

notes were in 1839, as they are at present, a legal tender. It is not pretended that coin was demanded in consequence of distrust of the ability of the Bank to pay its notes; on the contrary, it is supposed that the withdrawal of deposits was occasioned only by the desire to obtain coin because notes were withheld. But the depositors on demanding payment of their deposits, would have received notes, and having got what they desired, would not have required coin in exchange for them. The supposed motive to an internal drain of specie is entirely wanting.

(3.) The proposition that the circulation would be contracted of its own accord after the high price of corn and the adverse exchange had lasted sufficiently long to reduce consumption, and that such is the effect of these combined circumstances and not the result of any action on the part of the Bank, remains to be examined.

The phrase, "until the adverse exchange has lasted sufficiently long," begs the whole question. At what period will an adverse exchange affect a circulation governed by the laws which regulate a metallic currency? The answer will be—undoubtedly at the moment when that circulation is diminished by the exportation of coin and bullion, and to an extent proportionable to that exportation.

The argument of Mr. Wilson does not take cognizance of the management of the resources of bankers, and leads to the conclusion that, without reference to the amount of their reserves, notes or specie must be forthcoming until consumption abates. Let us then examine more particularly the causes of diminished consumption, and the means by which the circulation of the country is maintained.

It is truly said that high price of corn and adverse exchanges will ultimately diminish consumption. The question at issue regards the time and the mode in which these causes will operate.

When corn is dear more money is required to purchase it: that money can only be obtained by withdrawing it from other uses. Corn is an article of the first necessity, and in order to procure it when dear, men must dispense with luxuries and superfluities. The consumption of other commodities must therefore be diminished on such occasions in order to obtain corn. But the reduced demand for commodities will reduce production, and consequently the employment of labour, and prices in general, will be affected by these circumstances. These are the known effects of scarcity. They are occasioned by the withdrawal of money for the purpose of purchasing corn from foreign countries. Yet Mr. Wilson supposes that while money is in process of withdrawal, it may still be kept in circulation—nay, that it must be kept in circulation until consumption diminishes, and then, he says, money will disappear of its own accord. Is not this to reverse the cause and effect?

Again, it is said, an adverse exchange when it has lasted sufficiently long, will affect consumption, and then the circulation will, of its own accord, become contracted. In what way is it supposed that an adverse exchange affects consumption, if it do not first affect the circulation? Consumption is affected by prices, and an adverse exchange acts upon prices by means of a previous action on the circulation. If not counteracted, it would drain the country of bullion. It did so in fact in 1839, when the reserve of bullion in the Bank of England was only saved from exhaustion by means of a loan from the Bank of France.

As an adverse exchange, then, operates immediately on the basis of a convertible circulation, by what means is it supposed that convertibility can be maintained, if the amount of circulation cannot be affected by any action on the part of the Bank?

Some unaccountable confusion lurks in this proposition

regarding the means by which notes are maintained in active circulation. Independently of direct action on the deposits, bank notes can be procured by the public in two ways; namely, by taking bullion to the Bank and obtaining notes in exchange for it; or by obtaining advances from the Bank of a portion of those notes which are returned to it in the shape of deposits, or from the capital of the Bank. In administering to the wants of the public in these respects the Bank has, since the resumption of cash payments consequent on the Act of 1819, fulfilled two distinct functions, which, though not legally separated until the passing of the Act of 1844, involved a principle which could not be disregarded without endangering the stability of the institution.

The first-mentioned means of obtaining notes is of course inoperative during the continuance of an adverse exchange. Gold will not be brought to the Bank when it is required for export; on the contrary, gold will then be demanded from the Bank in exchange for notes. It would be inconsistent with the principle on which bank notes circulate to create additional notes in the face of a diminished quantity of gold. Mr. Tooke, Mr. Fullarton, and Mr. Wilson, all admit that convertible notes ought only to circulate as metallic money would circulate, and that any attempt to maintain an issue of notes payable on demand and coin combined exceeding the amount which would exist were the currency purely metallic, would only lead in the end to the return of the notes for payment. It is agreed, in short, that convertible bank notes can only be used as substitutes for coin. During an adverse exchange the only means at the disposal of the Bank for the supply of notes to the public, is derived from the deposits entrusted to it, or from its own capital; and the argument supposes that when the aggregate circulation is undergoing diminution, the Bank must draw upon the reserve upon which its solvency depends, in order to

afford the required supply of notes. It cannot, however, in reason be contended that it has no power of regulating the use of the deposits; that it must perforce discount bills or make advances on other securities without regard to the state of its reserve. Yet, the supposition that it must maintain an amount of circulation dependent on prices, leads inevitably to this absurd conclusion.

There are some minds, however, so insensible to reason, or so blinded by sophistry, that they will disregard the conclusions of legitimate deduction, and may perhaps consider that the facts on which Mr. Wilson's argument is founded, remain to be accounted for. Statistics have extraordinary attractions when they appear to lead to conclusions beyond the reach of ordinary intelligence; they then throw an obscurity over the subject which is mistaken for depth. On minds so constituted, the mistakes of a writer, enjoying deservedly a high reputation as a political economist, must have a fatal influence; it is due, therefore, to the cause of truth, to notice the inaccuracies of the figures quoted by Mr. Wilson in support of his opinions.

The statements on which his argument depends are—that the circulation of country banks having been increased from 11,364,000*l.*, in September 1838, to 12,275,000*l.*, in June 1839, was subjected to sudden contraction in consequence of the measures taken by the Bank of England at the latter date; and that the consequence of this contraction was a reduction of the bullion in the Bank of England from 5,119,000*l.*, which is distinctly stated to have been the amount on the 1st June, 1839, to 2,816,000*l.* in September following.

It appears, however, from the returns published in the Appendix to the Commons Report on the Commercial Distress of 1847, that the average circulation of country notes in the month of June 1839 was 11,502,963*l.*, instead of 12,275,000*l.*, as stated. It amounted to 12,519,753*l.*,

in the preceding month, and the great contraction to which Mr. Wilson refers had therefore taken place before the date assigned by him to the proceeding of the Bank to which he attributes it.

The following is the correct state of the accounts of the Bank of England at the two dates referred to, as they appear in the detailed statements published in the Appendix to the Report from the Select Committee on Banks of Issue in 1840:—

Week ending May 28, 1839.

		£	£
Circulation—			
London - -		13,556,000	
Branches - -		4,134,000	
			17,690,000
Deposits—			
Public - -		2,459,000	
Private - -		4,449,000	
			6,908,000
Securities—			
Public - -		12,396,000	
Private, viz.,			
Discounted bills	6,156,000		
Other credits	4,672,000		
		10,828,000	
			23,224,000
Bullion - - - - - -			3,910,000

Week ending September 3, 1839.

	£	£
Circulation—		
London - - -	13,789,000	
Branches - -	4,107,000	
		17,896,000

Week ending September 3, *continued.*

Deposits—			
Public - - -		2,069,000	
Private - - -		4,056,000	
			6,125,000
Securities—			
Public - - -		12,518,000	
Private, viz.,			
Discounted bills	7,938,000		
Other credits -	4,215,000		
		12,153,000	
			24,671,000
Bullion - - - - -			2,406,000

It appears from these accounts that the bullion in the Bank at the beginning of June 1839, amounted only to 3,910,000*l.*, instead of 5,119,000*l.*, as stated; that in September following it had been reduced to 2,406,000*l.*, instead of 2,816,000*l.*, as stated; and that the diminution in the amount during the three months was therefore 1,504,000*l.* instead of 2,303,000*l.*

It will be observed that during the period in question there was no such action on the deposits as had been ingeniously conjectured; the private deposits having undergone a diminution of only 393,000*l.* The true cause of the difficulties of the Bank will also be seen in the increased advances on private securities in the face of a continued drain of bullion.

The error into which Mr. Wilson has fallen arose from his referring to the quarterly averages instead of the actual state of the accounts at the dates in question. The quarterly average of bullion in the Bank of England to the 28th May, 1839, gives the amount which he quotes, viz., 5,119,000*l.*; but this is the average of the three months ending at that date, and it will be seen, on examining the

detailed accounts of the Bank of England, that this high average is owing to the comparatively large amount of bullion held in March 1839, after which month it began sensibly to decline, not suddenly as assumed, but gradually week by week. It is to be regretted that the enthusiasm of this eminent writer for a plausible theory should have led him to adopt, without sufficient reflection, figures which appeared to suit his argument, but which, on calmer consideration, he must perceive would lead to directly opposite conclusions.

Further opinions of "Economist" in 1855 and 1856.

The "Economist," in a series of articles from the 22nd of December, 1855, to the 19th of January, 1856, puts forward the same fallacy in a somewhat varied form. The Essays published by Mr. Wilson in 1847 contained arguments in support of Mr. Tooke's theory that prices govern the circulation, and endeavoured to show that a high amount of circulation must be maintained when trade requires it, even in the face of an adverse exchange and an export of bullion. The writer of the recent articles coincides, indeed, in the opinion that the Bank of England has no power to extend or contract the employment of money; but, reversing the argument that a large amount of circulation must be maintained in certain conditions of trade, he endeavours to show that "excessive credits, loans, and discounts" have no connection with the circulation of notes, and that, so far from "excessive issues" having been made in times of excitement, there was no increase of circulation at the periods of remarkable speculation in 1825, 1837, and 1847. He characterises the arguments employed by the supporters of the Act of 1844 as showing "obviously a confusion between currency and capital; between the issue of notes and the loan of capital; between circulation and credit:" and he endeavours to prove that the Act has failed in its object, because, in 1847, and in the autumn of 1855, the amount of notes with the public

did not, as he alleges, contract simultaneously with a diminution of bullion. In support of these views he furnishes extracts from the published Returns of the Bank of England at the periods referred to.

Reserving for the present the examination of that part of the argument which applies immediately to the operation of the Act of 1844, we will consider, first, the principles involved in these propositions, and then submit the statistics quoted in support of them to the ordeal of candid criticism.

The writer imputes confusion of ideas to the supporters of the Act of 1844, and, by way of elucidating the subject, contrasts currency, the issue of notes, and circulation, with capital, the loan of capital, and credit; regarding the three first and the three last, respectively, as synonymous terms. It is to be regretted that, in his zeal for accuracy, he did not explain the meaning which he attaches to a "loan of capital," or, as he subsequently expresses it, "floating capital," by a bank, and that he should have left to others the task of defining expressions which are placed by him, some in contrast, others in juxta-position, without apparent attention to the sense in which they are usually employed.

"Floating capital," as defined by political economists, is food and other wages of labour, materials, &c., employed in reproduction. It affords the means by which a country is enabled to carry on industry with advantage. The misapplication of that floating capital, or its withdrawal in case of deficient harvests, or other extraordinary demands, involves it in difficulty. This principle has been developed with great clearness in the "Economist" itself at different times. In what respect, then, can a bank be said to make an advance of floating capital? It cannot do so literally, because a bank does not deal in the materials of industry. It can only do so by affording the means of acquiring the use of floating capital,

or, in other words, by advancing money, or the value of money, which is the article in which a bank deals. The capability of a bank to promote the employment of capital must, then, depend on the amount of money at its disposal. If, by improvident advances, it encourages speculation at a time when the state of trade shows that speculation has already gone too far, the means of payment will fail, and the fund at the disposal of bankers will be diminished. If, in spite of this diminution of its resources, the bank continue to make advances tending to a further action upon its reserve, the state of indebtedness of the trading community must increase, the Bank will have difficulty in realizing its securities, the safety of the funds entrusted to it by depositors will be endangered, and the credit of the country will be shaken.

It is this state of things which the "Economist" probably contemplates when it employs the terms, excessive loans of capital, excessive credits, &c., in contrast to currency, issue of notes, and circulation, which it employs as synonymous terms, and regards as a service carried on independently of the employment of the means of extending credit at the disposal of the Bank. But in what sense are these terms used?

The inexactness of language in general favours the promulgation of vague and sophistical theories. There is no term employed in discussing questions of currency which can be used with so much effect for the purpose of obscuring meaning as the word "circulation." It is susceptible of different significations, and, according to that signification which writers choose to attach to it, may be employed at pleasure to draw distinctions, or to bring opposite things within the same category. Circulation, taken etymologically, may denote the act of circulating value, the active employment of the means by which value is circulated, or the means themselves—in other words, money or its substitutes. It would save much confusion

if the term were always used, in its technical sense, as synonymous with currency, to denote the circulating medium, consisting of coin and its substitutes; but both terms are vaguely employed by the "Economist" in the same category with "the issue of notes;" and from the figures which the writer quotes, it may be inferred that he considers the circulation to consist only of bank notes in use by the public.

A fallacy lurks in this restrictive employment of the term. Mr. Tooke and the "Economist" refuse to recognize the distinction between the functions of the Bank of England as issuers of notes and as bankers, and omit to take any account of the reserve of notes, the condition of which is the criterion of its management and the true index to the state of the whole circulation.

It will however be apparent, on consideration, that any discussion on the subject which treats of Bank of England notes in the hands of the public as distinct from those within the walls of the Bank, must lead to incorrect notions. Bank of England notes being a legal tender, and being (as has been already demonstrated) essentially a paper money, are held largely by other banks as their reserves: they constitute the principal means by which payments are made, and by which the balances of book-credits are adjusted. To consider, therefore, Bank of England notes held in reserve by private bankers as circulation, and to exclude from consideration those notes which are retained by the Bank of England itself for the same purposes, is a contradiction of terms. The amount of notes which are in active use, that is, which are passing from hand to hand daily in the course of trade, can never be clearly ascertained. The active employment of notes is one thing, the amount in existence is another.

Theoretical conformity between a convertible bank-note circulation and a metallic currency can only exist if

the circulation be considered in the light of money, and be taken to include the reserves of banks. In the case of a purely metallic currency, the operation of banking could not be carried on without a sufficient reserve of coin, and the quantity of money required for trade would be combined of that in use by the public and of that held in the coffers of banks. In order that notes should conform to this natural limitation, it would follow that the circulation should be understood as including the reserves of the issuing body. Notes paid into the banking department of the Bank of England become deposits for which it is responsible to the depositors, precisely as would be the case were they paid to any other banker. The aggregate value of the deposits mainly furnishes the fund which it employs for banking purposes. A considerable portion of that fund must, in prudence, be retained in readiness for the payment of demands; but if the bank continue to make advances from that fund, or, in other words, to lend its notes as freely as before, when the abstraction of bullion indicates a diminution of the quantity of the real circulating medium, it will, in fact, draw its notes from its reserve, whether the amount of that reserve be shown by the amount of notes held in the banking department according to the present mode of stating the accounts of the Bank, or be represented by the amount of unemployed deposits or notes acquired by the sale of securities and then cancelled, according to the former practice.

In fact, the conduct of the Bank on several occasions previous to 1844 betrayed a more serious dereliction of principle. Its issues, at times when the bullion had been reduced to a very low amount, must have not only exhausted its reserve by the reissue of cancelled notes, but must have involved a creation of new notes in the place of others returned for payment in specie.

It is impossible to attain a clear comprehension of

the working of our monetary system without giving due attention to the reserve of the Bank of England, which affords the most certain test of the prudence of its management. The amount of circulation required at different times depends on many circumstances, and bears no certain relation to the amount of deposits, or to the amount of bill transactions. The condition of the reserve is the truest indication of the immediate ability of the Bank to meet its engagements, and constitutes the gauge of its credit. Previously to the Act of 1844, the published accounts of the Bank afforded only imperfect information regarding the real position of the Banking Department, and it augurs ill for the judgment of the objectors to that measure, that they refuse to take cognisance of the existence of the reserve, and invariably discuss the question as if there were an inseparable connection between the functions of issue and banking when conducted by the Bank of England. Such a notion would not be entertained for a moment in the case of any other bank, and it has yet to be shown that the position of the Bank of England exempts it in any respect from those requirements in the management of its business which apply to every cognate institution.

The "Economist" treats the bullion as the real reserve of the Bank: but in this view it overlooks the fact that the Bank of England has now no power in the management of the issue department, and that, as regards the circulation, the bullion is equally the reserve of all the banks that employ its notes; that in fact the Bank has neither more nor less access to the bullion than any other banker, their position being essentially the same and differing only in name. Yet allowing, for the sake of argument, the correctness of its opinion, there is manifest inconsistency in the notion that, even before the Act of 1844, the Bank had power over the bullion but none over the circulation. The bullion furnishes the means for the payment of notes on demand. If the same amount of notes

be employed while the bullion is undergoing diminution, as were employed before such action upon the bullion commenced, the proportion between the notes and the bullion would be altered; the security for the payment of the notes would be lessened; the Bank would be advancing a larger amount of notes upon credit, with fewer notes within its command, and that larger amount would be drawn from its banking reserve.

The "Economist" (and it may be added Mr. Tooke) recognizes the importance of maintaining an ample stock of gold, as a fund for the payment of notes, and uses the following emphatic expressions on the subject:—

"No one who contends for convertibility will deny that it is the duty of the issuers of notes, to retain in their possession at all times such a reserve of that commodity in which their notes are payable, as will enable them to fulfil their obligations."

Entertaining this opinion, can the writer contend that the amount of bullion necessarily held by the Bank under the operation of the Act of 1844 has been excessive? If he consider it excessive, he is bound to state the amount which ought, in his opinion, to be held in deposit as a sufficient security for convertibility; and he is further bound to state the course of action by which the Bank, were its power of issue unrestricted, could maintain such amount of bullion as he may consider sufficient, if, as he contends, it have no power of controlling the quantity of notes in use by the public.

He cannot do this. He admits the principle that, with legal convertibility, bank notes if issued in excess will be returned for payment; but he denies that the Bank of England has the power of regulating the quantity which may be employed by the public. He asserts, at the same time, that the duty is imposed on the Bank of main-

taining an ample reserve of gold, which reserve is liable to be acted upon by the return of notes for payment. He recognizes, therefore, an obligation; but denies that the power of fulfilling it exists.

It is time now to refer to the statistics by which the writer attempts to support these contradictory conclusions. His objects are to prove that there were no excessive issues at times of great speculation, and that bankers have no power to increase or diminish their circulation at pleasure. The following are the figures (quoted with his comments) upon which he relies for these conclusions:

"First, from the calm and depressed period of 1821 to the most excited moment in 1825, the facts were as follows:—

	Circulation.	Advances on Private Securities.	Bullion.
	£	£	£
August 1821 ...	20,295,000	2,722,000	11,233,000
August 1825 ...	19,398,000	7,691,000	3,634,000

"The public securities had also been increased in the meantime from 15,752,000*l.* to 17,414,000*l.*

"Let us next make the same comparison of the calm and depressed period of 1833 with the excited period of 1837:—

	Circulation.	Advances on Private Securities.	Bullion.
	£	£	£
February 1833 ..	19,370,000	5,450,000	9,500,000
February 1837 ..	18,232,000	15,065,000	4,089,000

"Next for the speculative period of 1847 as compared with the sober times in 1844:—

	Circulation.	Advances on Private Securities.	Bullion.
	£	£	£
February 1844 ..	21,148,000	5,837,000	16,213,000
August 1847...	18,828,000	16,923,000	9,163,000

"These figures are taken from the Bank Returns in the Appendix to the Report of the Committee on Commercial Distress, 1848, at pages 8 and 9. In every case, the circulation, in place of being "excessive" at the moment when speculation was at the highest point, was somewhat less; but in every case had the advances upon private securities enormously increased, and the amount of bullion enormously diminished. What, then, had bank notes to do with these convulsions?"

The first series of the articles on the subject, in which the quotations of the state of the circulation in the periods above referred to were given in greater detail, contained also the following reference to the circulation of the autumn of 1855:

"Again, turning to the drain of the last autumn. The following are the returns of the bullion and the circulation of notes in the hands of the public in each week from the 23rd of June, when the bullion was 18,169,000*l.* to the 13th of October, when it had fallen to 11,752,000*l.*:—

Month ending		Bullion.	Notes in Circulation in the hands of the Public.
1855		£	£
June 23	...	18,169,000	19,542,125
June 30	...	18,019,000	20,165,545
July 7	..	17,584,000	20,482,750
July 14	...	17,329,000	20,978,870
July 21	..	16,644,000	20,772,865
July 28	...	16,385,000	20,964,845
August 4	...	16,232,000	20,709,290
August 11	...	16,275,000	20,493,430
August 18	...	16,117,000	20,277,140
August 25	...	15,546,000	20,042,215
September 1	...	14,939,000	20,104,630
September 8	...	14,217,000	20,142,105
September 15	...	13,698,000	19,713,470
September 22	...	13,269,000	19,408,435
September 29	...	12,939,000	20,172,685
October 6	...	12,279,000	20,281,551
October 13	...	11,752,000	20,648,365

"The bullion in the Bank stood on the 23rd of June at 18,169,000*l.*; it gradually but quickly fell to 11,752,000*l.* What was the fate of the circulation? Did it contract according to the theory of Sir Robert Peel, and which the Bank Act of 1844 was to accomplish; or did it expand, as the practical bankers said it must? With the bullion at 18,169,000*l.* the circulation was 19,542,000*l.* With the bullion reduced to 11,752,000*l.* the circulation had risen to 20,648,000*l.*"

We have thus statements regarding the condition of

the circulation (according to the restricted acceptation of the term allowed by the "Economist" which ignores the banking reserve) at two periods before any restraint was placed on the issue of bank notes, and at two periods after the passing of the Act of 1844.

It would, indeed, have been a startling fact, if after all that had been said, in and out of Parliament, about the excessive issues of notes in 1825, it had turned out as represented by the "Economist," that the circulation was somewhat less in that year than it had been in 1821; but in arriving at this conclusion the writer has omitted some material circumstances. His comparison of the circulation of the Bank of England itself is made on a false principle, as will appear from the following details:—

	Bank notes of £5 and upwards, and Post-bills.	Bank notes under £5.	Total Circulation.
	£	£	£
31st August, 1821 ...	17,747,070	2,548,230	20,295,300
31st August, 1825 ...	19,002,500	396,340	19,398,840

With these figures before him, he has failed to observe the important fact that the apparent diminution of the circulation of the Bank of England was owing to the withdrawal of 1*l.* notes, and the substitution for them of gold coin within the district of its exclusive privileges, and that the circulation of bank notes and bills of 5*l.* and upwards in 1825, the only point of just comparison, shows an increase of 1,255,430*l.* over that in the corresponding period of 1821. But this is not all: the writer refers to a period of the year 1825 when a considerable contraction of the circulation, the forerunner of the impending crisis, had already taken place. The returns of an earlier month, quoted with others in a previous number of the "Economist," would have afforded a more conclusive comparison;

and he had before him a statement from which it appears that on the 28th February, 1825, the amount of notes of 5*l.* and upwards, and post bills issued by the Bank of England, was 20,337,030*l.*, being an increase of no less than 2,889,670*l.* over the amount of these instruments in the corresponding month of 1821. With still greater disregard of any facts except those which suit his argument, he has omitted to bear in mind the excessive issues by country banks in 1825, increasing simultaneously with those of the Bank of England, to the extent of about 33 per cent., as stated by Lord Liverpool, and amounting, according to the estimate of the same statesman, to an addition of no less than 4,000,000*l.* to the aggregate note circulation of the country.*

Unmindful of these circumstances, the writer in the "Economist" expresses surprise at the subsequent increase in the circulation of the Bank of England. "What is most striking," he observes, "is, that notwithstanding the slight variation in the circulation during the great excitement of 1825, when speculation was so rash and credit so indiscriminate, after the greatest possible restriction had been placed upon credit in December and January, the circulation of the Bank had risen, on the 28th of February (1826), to 25,476,000*l.*, including the million of 1*l.* notes then issued." Is it possible that an instructor of the public on a subject which requires, more than any other, calm and patient investigation, should be ignorant or unmindful of the fact, that this exceptional increase of issue on the part of the Bank of England was made in order to supply an adequate amount of circulating medium in the country, which had been brought "within a few hours of a state of barter," by the

* Mr. Tooke estimated the increase of the country note circulation at this period at 7,000,000*l.*; but as he was then enthusiastic on the opposite side of the question from that which he has since adopted, it is the safe course to adhere to the more sober estimate of Lord Liverpool.

failure of seventy banking establishments within six weeks, and the sudden destruction of six or seven millions of country notes?

In like manner, when he refers to the decrease of the circulation of Bank of England notes in 1837 as compared with 1833, he omits all reference to the simultaneous increase in the issues of country banks. Mr. Wilson, in his essay written in 1845, dwelt on this circumstance in reference to the circulation of 1838, and employed it, with what success we have seen, in support of his argument, that the circulation could not be diminished by the action of the Bank. It accords with the present argument of the "Economist" to regard the circulation of 1837 as having undergone diminution, and the writer suppresses the fact of the increase of the issues of private and joint-stock banks at this period. The monthly average issues of those banks amounted in September 1833, the date of the first published return, to 9,585,644*l.*; in February 1837, they had been increased to 10,848,801*l.* The total average amount of bank notes issued in the United Kingdom in the month of September 1833 was 36,035,244*l.*, and in February 1837, 38,037,382*l.*,* showing an increase in the period of 2,002,138*l.*, notwithstanding the great diminution of bullion to which the "Economist" refers.

Turning now to the circulation at the periods referred to subsequent to the Act of 1844, and which it may be observed, in passing, the writer treats as unaffected by the restrictions of that Act, it is sufficient to remark, with reference to the statement regarding the year 1847, that it is manifestly incorrect to describe that year as "a period of speculation." It was a period of collapse after the fever of the preceding year, and in the month of August the country had partially recovered from one panic and was on

* *Vide* Appendix No. 1 to Commons' Report on Commercial Distress, 1848.

the eve of another. It will be necessary to refer hereafter more particularly to the position of the Bank in that year.

The remarks on the drain of bullion during last autumn, afford one of the most striking examples of the short-sightedness with which writers of this school seize upon facts which appear to favour their fallacies, and, having obtained them, rest contented without further investigation. It is correctly shown that on the 23rd June, 1855, the bullion in the Bank amounted to 18,169,000*l.*, and that from that time it underwent a progressive diminution, until the 13th October following, when it was reduced to 11,752,000*l.*; but that in the meantime the amount of notes with the public had increased from 19,452,000*l.* at the former, to 20,648,000*l.* at the latter date. Upon which the question is triumphantly put with reference to the circulation, "Did it contract according to the theory of Sir Robert Peel; or did it expand, as the practical bankers said it must?" We have here a misstatement of the theory on which Sir Robert Peel's Act was founded; but reserving that point for future observation, we have the opposite theory, broadly stated, that the circulation (in the sense in which the word is used by the writer) must expand, under the conditions in which the Bank of England was placed at this period.

Now, the article from which the quotation is extracted, was published on the 29th of December, 1855, and it may be asked why the writer, with the published accounts of the Bank of England before him to the 22nd of that month, stopped short at the date of the 28th of October? The answer may probably be found in the circumstance that Mr. Tooke, having referred in his pamphlet to the latter date, and found figures that appeared to favour the theory advocated, any further investigation might have proved inconvenient. It will be well, however, for the sake of sound principle, to supply the omission. From the 20th of October to the 22nd of December, 1855,

the amount of bank notes in the hands of the public underwent a rapid diminution from 20,371,745*l.* to 18,379,690*l.*, and the reserve of notes in the banking department was increased at the same time from 4,310,485*l.* to 6,464,705*l.* The reason for this altered aspect of the state of the accounts of the Bank is easily accounted for from facts faithfully recorded in the "Economist," and within the knowledge, therefore, of the author of the article when he wrote it, if he had turned his attention to them. The Bank, observing the diminution of its reserve, took measures to check its advances on securities by raising the rate of discount. The minimum rate was successively raised on the 8th, 15th, and 29th of September and the 6th of October, 1855, to 4, 4½, 5, and 5½ per cent.; but these measures having proved ineffectual, the rate was further raised, on the 20th October, to 6 per cent. on some descriptions, and to 7 per cent. on other descriptions of paper. The "Economist" announced, with some parade, the opinion that there is but one sound remedy to check "excessive advances,"—a remedy of which, as it states, "theory and experience alike show its efficacy, namely, AN INCREASE IN THE RATE OF INTEREST." This remedy may not be effectual under all circumstances without other measures of precaution; but there can be no doubt that it was so at the particular period referred to. It did on this occasion, for a time, check advances; but as a natural consequence, which the "Economist" fails to perceive, the Bank, having advanced fewer notes, had a larger amount in its till, and the public had consequently a smaller amount in its hands.

It is no part of the duty of the Bank, under the Act of 1844, to regulate the issue of notes. Their duty, like that of all other bankers, is to protect their reserve, and, if they fulfil that duty, the circulation will take care of itself. The inevitable result of an increase of the reserve, arising

from a contraction of advances, must be a diminution of the quantity of notes in the hands of the public, unless deposits be diminished in a corresponding ratio. This is a proposition so undeniable, so palpably true, that sophistry itself could hardly gainsay it; and although the "Economist" alleges that "practical bankers" are of opinion that, under conditions, such as those in which the Bank was placed last autumn, the circulation must expand, we may be permitted to doubt whether any banker of really practical experience would assert a proposition so opposed to reason and proved results.

Summary of the preceding propositions.

Before entering upon the practical considerations which will afford the real test of the expediency of the Act of 1844, it will be instructive to exhibit in a concise summary the various theories which have been under consideration, and thus to bring them into direct contrast with each other. They may be reduced to the following propositions:

1st. That bills of exchange belong to the same category with bank notes, and generally increase in amount as the latter diminish.*

2ndly. That, with legal convertibility, bank notes must necessarily fluctuate in conformity with the principles which govern the supply of the standard metal,† and belong, therefore, to a different category from bills of exchange, which are said to fluctuate in an opposite direction from bank notes.

3rdly. That prices govern the circulation,‡ and that bank notes do not, therefore, fluctuate in conformity with the laws which govern the supply of the standard metal.

* Mr. Tooke's pamphlet, pp. 20 and 22.

† Mr. Fullarton, quoted by Mr. Tooke in pamphlet, p. 53. "Economist," April 5, 1845.

‡ Twelfth of series of "Conclusions," published by Mr. Tooke in 1844. "Economist," April 12, 1845.

4thly. That a large amount of circulation must be provided when great activity of trade prevails, and that if bank notes be withdrawn from the public at such times, coin will be obtained to supply their place, even in the face of an adverse exchange.*

5thly. That, contrary to the last proposition, so far from a large amount of bank notes being required in times of great activity of trade, the circulation is generally more contracted in such times than in quiet times.†

6thly. That banks of issue have a power of contracting the circulation of their notes, but have no control over their reserve of specie.‡

7thly. That, nevertheless, it is the bounden duty of such banks to maintain an ample reserve of specie.§

It has been shown that every one of these propositions, except the last, is in itself false; but it is further evident that each is inconsistent with the rest. It is no wonder if an ingenious mind, when treating of an intricate subject, should become involved occasionally in a fallacious argument; but the philosophy is past comprehension which induces a class of writers to adopt, deliberately on principle, and with a view to system, a series of propositions at once unsound in themselves and contradictory of one another.

* "Economist," April 12, 1845, and December 22, 1855.

† Ibid., December 22, 1855.

‡ Ibid., April 12, 1845.

§ Ibid., December 22, 1855.

SECTION VI.

NECESSITY FOR STATE CONTROL OVER THE NOTE CIRCULATION; REVIEW OF THE EVENTS WHICH LED TO THE ADOPTION OF THE ACT OF 1844; THE SCOPE AND INTENTION OF THAT ACT; AND ITS RESULTS.

Necessity for control by the State over issues of bank notes.

If the writers who raise hypothetical objections to the principles of the Act of 1844 felt confidence in their own theories, they should advocate entire freedom in the privilege of issuing bank notes. Were it true that these instruments cannot be issued in excess, there would be no motive for restriction upon their use, further than such as some reasonable precautions for securing convertibility might demand. Yet no one has hitherto proposed to carry this principle into full effect. No one, for example, has advocated the extension of the privilege of issue to joint-stock banks in London, institutions of undoubted stability, or to the wealthy private bankers in London, whose position and credit are equally above question. A reserve has been observed upon these points, which shows a commendable regard for practical considerations, while it betrays at the same time distrust on the part of the writers in their own speculative opinions. In truth, the commercial history of every State, in which this expedient of economizing metallic money has been adopted, affords abundant evidence of the necessity for legislative interference to check its abuses. The volumes of Adam Smith relate instances of practices which had prevailed in this country and in Scotland, at that early date, of so objectionable a character as to require the intervention of Parliament. In the United States of America, where the popular feeling in favour of a free paper circulation is probably stronger than in any other country, the legislation on the subject exhibits a series of experiments to prevent the excesses which had

been the consequence of this freedom. Even the advocates of 1*l.* notes do not propose that we should revert to the shilling notes which once circulated in the north of England, and were suppressed by legislation.

The necessity for some restriction may be held to be universally admitted, notwithstanding the theoretical arguments advanced to prove that it is not required. The question becomes, therefore, one of expediency as to the extent to which that restriction should be carried. And this affords a conclusive answer to the objections which have been lately urged by Mr. Tooke and others against the statute of 1844, on the ground that it involves an exercise of authority by the State exceeding its proper functions. Mr. Tooke represents the advocates of the Act to be of opinion "that the function or business of creating or issuing promissory notes, payable to bearer on demand, is an indefeasible attribute and province, or prerogative, of the Sovereign or State;" and he proceeds to argue against this position. We have here one of those exaggerations which may serve to withdraw attention from the real principle in dispute, but are unworthy of a writer who affects a tone of philosophy. It has never been contended that the right of issuing notes is inherent in the Sovereign or State in the same sense as the prerogative of coinage; but, nevertheless, the reason that has led to an universal recognition of that prerogative, may properly lead to the regulation or suppression by the State of any medium, not possessing the desirable qualities, which may be used as a substitute for the coin of the realm.

Opinions may differ as to the duty of the State in regard to the degree of protection which it should afford to the community from the consequence of reckless or fraudulent transactions in trade. But whether it be prudent or otherwise to leave banks the unfettered power of dealing with the funds entrusted to them, it is evident that the character of the obligations which they incur with their immediate

customers, is widely different from those which arise from the use of promissory notes payable to bearer on demand. The deposit of a sum of money with a banker, the negotiation or acceptance of a bill of exchange, and other transactions of that nature, are acts performed on the faith of individual credit and with the knowledge of the risk incurred; but bank notes, which circulate from hand to hand as money, are received, in payment, not from individual confidence in the issuer, but on the assurance of common faith, in some measure also without the real power of choice, as no trader could refuse payment in that medium of exchange which every one is willing to accept. If it be the duty of the State to preserve the metallic money from deterioration in value, it would seem that a like obligation would arise in the case of a paper currency which is allowed to be used in place of the coin of the realm; and, beyond controversy, this obligation must apply in the case of the notes of the Bank of England, which, for reasons of public policy, were made a legal tender, and which, therefore, every one is obliged to accept in payment as freely as the coin which bears the stamp and effigy of the Sovereign.

Mr. Tooke once expressed himself on this subject in those energetic terms with which he is in the habit of enforcing his opinions, and which are particularly observable on occasions when he seems to condemn, by anticipation, his later fallacies. Referring to the question of publicity of accounts, he observed to the Committee of 1832, on the Bank of England Charter:—

"As to the right of requiring it on the part of the public, there is no question, because the privilege of issuing paper money is a delegation of that which is universally considered as a privilege residing in the State." (Qu. 3,919.)

And again: "That strikes me to be a most extraordinary circumstance connected with the country issue of

paper money, that whereas Government invests with a number of sanctions, the privilege of issuing coin upon the intrinsic metal, by which nothing is to be gained, it should allow individuals the privilege of coining it upon a material which in itself is worth nothing, and consequently upon which there is a very great gain by the substitution of it for the other, which is of intrinsic value." (Qu. 3,939.)

Opposing influences of the Bank of England and country banks before the Act of 1844.

It was observed in the outset that the subject divided itself into two parts, namely, the question of the exercise of an unrestricted power of issue by banks acting independently of each other, and that of the position of the Bank of England as a controlling body.

In the course of the preceding discussion on opinions advanced in the "Economist" by Mr. Wilson, allusion has been made incidentally to the conduct of the country banks in increasing their issues at times when the Bank of England had attempted to contract the circulation. The latter institution was itself very far from being free from blame in the management of its issues at various periods, but it is admitted by Mr. Wilson that, on occasions when the Bank became sensible of the necessity for stringent measures, the policy which it endeavoured to follow was thwarted by the opposing action of other issuing bodies. The effect of this conflicting influence will be best illustrated by a reference to the times of monetary derangement which have occurred since the resumption of cash payments under the Act of 1819; and attention will naturally be directed to the crisis of 1825 and its causes, and to the difficulties which extended, at recurring intervals, from 1834 to 1839.

Speculation ending in the crisis of 1825.

It has become a practice with the opponents of the Act of 1844, to underrate the effect of ill regulated and excessive issues of bank notes, and, depending much on forgetfulness of past difficulties, to ridicule the notion of

their being attributable in any important degree to mismanagement of the circulation.

The disasters of 1825 originated in a mania for investments in foreign loans, and afterwards in joint-stock companies of various descriptions, but chiefly in bubble undertakings for working mines in South America. To those who have not followed the ramifications and connections of mercantile transactions, it might not appear probable that speculations in foreign undertakings would have an immediate effect on the internal trade of this country; but it must always be borne in mind that money is but the medium by which commodities or capital are interchanged, and that foreign investments are effected by the withdrawal of capital from employment at home. Speculative engagements exceeding the floating capital disposable create a demand for capital beyond the power of supply, and, to the extent to which they may be carried, lead to an unhealthy action and stimulus to trade throughout the community. The evidence before the Committee of 1832, on the Bank of England Charter, affords ample proof of the feverish excitement which generally prevailed in 1824 and 1825, extending to the remote parts of the country, and influencing even the fairs and cattle markets of Wales.

Such increased trade could not have been maintained without an increased circulating medium; that medium, which could not have been supplied by metallic money, was furnished by excessive issues of notes. The Bank of England lent itself to the prevailing influence; but the main cause of the disastrous reaction which occurred at the close of the year 1825 was the conduct of the country banks. The situation of the Bank at this period is thus described by Mr. Norman:—

"The situation of the Bank in December 1825 did not take place from an internal discredit applicable to the notes of the Bank of England; it arose from an internal discredit applicable to the notes of other issuing bodies,

especially those of 1*l.* and 2*l.*, which could only be paid in gold. The private bankers required gold to pay their notes, and in endeavouring to obtain this gold they almost drained the coffers of the Bank."*

The debates in Parliament in 1826, when the recent disasters were fresh in men's minds, afford ample corroboration of the views above stated, and convey the opinions of statesmen whose authority cannot be disregarded.

Lord Liverpool observed, that "speculations in trade had been the origin of the evil, but it would not have been so extensive if it had not been aided by the state of the currency." †

And again, "The exchanges do not depend on the circulation of the Bank alone, but on the circulation of the Bank and country generally. The whole paper of the country should be taken into consideration."‡

Lord Lansdowne observed: "It was manifest that between the currency and speculation there was a mutual action and reaction. He found an issue from the Bank increasing in the ratio of 8 per cent. from 1824. He also found in 1825, after the Bank issues had increased, that the issue of country bank notes had been increased about 33 per cent. Gold, in consequence, rapidly left the country."§

Mr. Huskisson, after referring to the overtrading which had been carried on, called the attention of the House of Commons to its effect on prices, in the following passage:—

"Let the House but consider for a moment what had been the effect of that overtrading. It produced a rise in prices so rapid that it had never been equalled. And what was the consequence? Why, a fall as rapid and unequalled as the rise had been."||

* Evidence before the Committee on Joint Stock Banks, 1840. (Qu 2,269.)

† Lords' Debate, February 17, 1826.

‡ Ibid.

§ Ibid.

|| Commons' Debate, February 10, 1826.

He illustrated this assertion by detailed quotations of the market prices of various articles, at the time referred to.

One more extract from the speech of a statesman, the late Lord Ashburton, whose opinions every one must regard as bearing great weight, but whose authority ought to be held in especial respect by the opponents of the Act of 1844, will complete the illustration of the subject:—

"He (Lord Ashburton, then Mr. Alexander Baring) had no hesitation in attributing that distress to the extent to which the circulation of paper money had been pushed about eighteen months ago, and for which the country banks, and he was sorry to say the Bank of England, was answerable. The Bank of England, by the facilities which they afforded, had been the authors of that redundancy of money that gave rise to the wild speculations which some time ago abounded in every part of the country. The country banks had added to this redundancy in a much more mischievous manner. The Bank of England exercised a discretion as to the quantity of paper which it had put out; but the very business of a country bank was to put out all the paper it could; and this, as every gentleman acquainted with country banks well knew, was their constant practice."

After mentioning the manner in which country bankers proceeded, in order to withdraw from circulation the paper of the Bank of England, and substitute for it their own, Lord Ashburton, proceeded to observe:—

"By these means the country was saturated with paper-money, and that redundancy produced which had been the parent of the existing distress. And all this had been done without the least reference to the effect which it must necessarily have upon the exchanges, which, as persons acquainted with the nature of such things well knew, should be the regulation for the issue of paper-money."*

* Commons' Debate, February 2, 1826.

The evil, of which the whole country was sensible in 1825, was the sudden prostration of credit by the failure of numerous banks, and the individual losses which spread far and wide among the population, which, having received bank notes as money, found that they possessed only worthless paper. Parliament endeavoured to guard against the recurrence of this evil by preventing the further issue of bank notes under the value of 5*l.*, and by encouraging the establishment of joint-stock banks with paid-up capitals and responsible bodies of proprietors. These measures were improvements on the former practice; but subsequent events proved them to be insufficient for the object in view of establishing a sound system of circulation.

Period from 1834 to 1839.

After nearly ten years of quiet, the elements of disturbance began again to operate, and a drain of bullion commenced in 1834, which is attributable to large investments in foreign loans. The monthly average of bullion, which was 10,120,400*l.* in December 1833, was reduced to 6,062,000*l.* in April 1835. The circulation of Bank of England notes during that period remained undiminished, and that of the country banks increased from 9,778,304*l.* in December 1833, to 11,023,301*l.* in April 1835. A panic ensued in the latter year. After a slight reaction the drain of bullion recommenced in 1836. The bullion in the Bank was reduced on the 7th of February, 1837, to 3,831,000*l.*, and a commercial crisis ensued. The difficulties of the Bank at this period commenced with banking discredit in Ireland, in the autumn of 1836, which led to aid being afforded to the banks of that country by the Bank of England, by the transmission of gold from London. The Northern and Central Bank of England (a bank of issue), having a central establishment at Manchester, and thirty-nine branches scattered throughout the manufacturing districts, became involved in difficulties later in the year,

and assistance was afforded to it by the Bank of England, on consideration of the danger to be apprehended in the event of a suspension of payments of such numerous banking agencies at one and the same time. Discredit extended in the following year to the banking interests in London, and the American houses in London and Liverpool became embarrassed; aid was given to many of these houses, and the advances by the Bank on account of all these transactions exceeded at one time 6,000,000*l.** During this period the circulation of the Bank of England was maintained at its former level, while that of the country banks had been increased to an amount exceeding 12,000,000*l.* in December 1836. After the difficulties of 1837, a reaction commenced, and by the 28th of February, 1838, the bullion in the Bank amounted to 10,524,520*l.* The Bank, flushed with prosperity, resorted at this period to the anomalous proceeding of remitting gold to America; but the prosperity was short-lived: unprecedented imports of foreign corn created unfavourable exchanges. A steady drain of bullion set in, the amount of which was reduced on the 31st of August, 1839, to 2,404,540*l.*, and the Bank of England was brought to the discreditable necessity of resorting to the Bank of France for a loan, in order to preserve even that amount in its coffers. During this time the usual phenomena attending the issue of country notes, when unrestricted, are observable: in the month of February 1838, when the bullion was at its highest amount, the average amount of country notes in circulation was 10,690,549*l.*; from that time, in the face of a drain of bullion, the issues increased, until the monthly average amounted in April 1839 to 12,662,312*l.* The efforts of the Bank of England to check these proceedings of the country banks, after it had itself become sensible of the necessity for a

* Mr. Horsley Palmer's evidence before the Committee on Banks of Issue, 1840. (Qu. 1,285, *et seq.*)

contraction of the circulation, have already been considered.

It is observable that during the recurring difficulties which extended from 1834 to 1839, confidence on the part of the public in the ability of the issuing bodies to pay their notes was not generally disturbed, and in this respect the period offers a striking contrast to the crisis of 1825. At both periods the credit of Bank of England notes was maintained.

Mr. Wilson availed himself of this fact in his cross-examination of the Governor and Deputy-Governor of the Bank, before the Committee of the Commons on the commercial distress of 1847, and endeavoured adroitly to fix them to the admission that the convertibility of the notes was never endangered by the proceedings of the Bank. The "Economist," in its recent articles, takes up the same view and asks, "Was there ever a moment between 1819 and 1844, when the solvency of the Bank of England was disputed, or its notes discredited?"

It is, however, a narrow and incorrect view of the question to contend that, because the public is willing to receive bank notes in payments, the community at large suffers no injury from their over-issue and consequent depreciation. It has been observed by Mr. Norman, with reference to country bank issues, when they were unrestricted, that "a wealthy banker may mismanage his issues without danger to himself by keeping a sufficient reserve of securities in London."* This is not mere conjecture; the evidence of Mr. Wilkins, a country banker at Brecon and Merthyr Tydvil, before the Committee of 1832, affords a striking example of issues conducted with a view to individual advantage when the issuer was aware that the reckless proceedings of other banks "could not tend to good." In this case the issues were sustained by a reserve of public securities, which were ultimately sold at

* Evidence before the Committee on Banks of Issue. (Qu. 2,026.)

a loss.* Convertibility may be maintained under such circumstances, even when the issues are so conducted as to cause a violent and unnatural action upon prices.

The case with the Bank of England is, in some respects, different. That institution, as the banker of the Government and the manager of the National Debt, is the centre of the monetary system of the country. Its notes, being a legal tender, may be employed by other banks as money, and bear, therefore, a more immediate relation than other bank notes to the great reserve of bullion on the credit of which they are issued. Convertibility is essential to the maintenance of their relation to the reserve of bullion, and if, in consequence of over-issue (antecedently to the Act of 1844), that reserve were reduced to too low a proportion to the amount of circulation, the credit of the country would be endangered. But the public faith in Bank of England notes might, notwithstanding, be in a measure maintained, so that they might still be received in payment without hesitation, and so that no inducement might arise for a run upon the Bank for gold coin, for the purposes of internal circulation. A powerful body like the Bank of England might, in an extreme case, save itself from bankruptcy by an effort which would shake the general credit of the mercantile community, and, in spite of mismanagement of its circulation, that sort of faith in its solvency might be maintained which would arise from confidence in the general stability of the institution and in the Government with which it is connected: that faith would be of the same character as the confidence which induced the public to receive Bank of England notes during the suspension of cash payments. It can hardly, however, be alleged that, when the Bank was answerable for the payment of notes amounting to 17,896,000*l.*, and had no more than 2,406,000*l.* of bullion to meet any demand

* Evidence before the Committee of 1832 on the Bank of England Charter. (Qu. 1,642—1,667.)

upon it, which was its state on the 3rd September, 1839, it was in a safe and creditable position, or could have maintained the convertibility of its notes if circumstances had caused such a run upon it as arose in 1797. Still less can it be considered consistent with public faith, that Bank of England notes should be made a legal tender unless their convertibility be fully secured.

The effect of over-issue is to maintain prices for a time above their natural level, and to sustain individual credit, perhaps also for a time only, at the cost of the community. Gloss over the fact as we may, the fact nevertheless remains, that an issue of notes, exceeding the amount which a pure metallic currency would supply, is a creation of paper money on credit, the cost of which devolves on the country at large, by the high prices which it occasions, and the consequent loss of bullion which can only be restored by measures of restriction, the effect of which is in the end aggravated by being postponed. But is it true that the solvency of the Bank was unquestioned during the period to which we have been referring? It may be that its discredit did not lead to any internal demonstration; but we have the evidence of an unimpeachable witness that it was felt on the Continent, and operated there most prejudicially to the interests of this country. Mr. Horsley Palmer attributes the continued drain of bullion in 1839 to the following, among other causes; namely, "doubt existing upon the Continent, after May and June 1839, of the ability of the Bank to maintain specie payments, and, in consequence of such apprehension, the transmission of all long dated bills upon this country for immediate discount."*

In the vain attempt to save the credit of the country from the consequences of over-trading, the Bank adopted measures which led to general distrust. No violent convulsion ensued in 1839 as in 1825, but the country fell into a state of collapse from exhaustion. A

* Evidence before the Committee on Banks of Issue, 1840. (Qu. 1,362.)

long stagnation in trade ensued. Distress in the manufacturing districts was soon felt, and its attendant evils, political excitement and civil commotion. The gloom of the few years that followed 1839 has passed away, but the discontent of that time was only appeased by the overthrow of a Ministry and the ultimate triumph of the principles which it had advocated.

Principles of the Act of 1844.

The frequent recurrence of derangement in our monetary system impressed many well-informed and thinking men with the growing conviction that the management of the circulation could not, with safety to the public, be entrusted to individual discretion. Wealthy banking companies, no less than private bankers, were found to be governed by narrow views of immediate profit, and to disregard the principle, the soundness of which was admitted in theory, of regulating the circulation of their notes by the state of the exchanges. The Bank of England was frequently compelled, as in 1825 and in 1836, to weaken its own resources in order to save the country from the evil consequences of over-issues by other banks. The Bank itself, while thwarted in its tardy attempts to control the circulation, was in general governed, in the management of its own issues, by no well-defined system. It encouraged in the first instance, as was remarked by the late Lord Ashburton, the insane speculation of 1824 and 1825; it almost invariably delayed any precautionary measures during periods of commercial excitement, or of impending difficulties, until the necessity arose for stringent action in order to save its own credit; and in 1839 it resorted to a proceeding, with a view of mitigating the consequences of unfavourable exchanges with the United States, entirely at variance with sound principles of banking. In times of commercial embarrassment, which had been induced by previous irregularities, the Bank considered it a duty to employ its resources to the utmost in

order to aid other banks or mercantile houses which were in difficulty. An impression generally prevailed that at such periods the credit of the Bank was available as an ultimate resource. Thus a feeling of dependence was created injurious to healthy action in trade and inimical to habits of forethought. Credit was by this course further strained in the effort, often unavailing, to save houses already tottering under the effects of its abuse. The issues of bank notes employed for this purpose extended the depreciation of the currency, and the re-action was rendered in the end more violent from having been too long delayed. The assistance afforded by the Bank, necessarily irregular in its operation, often favoured those whose improvidence had led them into difficulty, and the pressure which but for its interference might have been confined to unsound houses, was entailed upon others from no fault of their own, and was spread more widely and generally over the community at large. On the other hand, the relation of the Bank to the Government sometimes rendered it difficult for that institution to persevere in a prudent course of action, when it was so disposed. Depression in the money market will often interfere with financial operations, and when a discretion rested with the Bank, occasions would arise when it would be difficult to exert it prejudicially to the immediate objects of its best customer.

The evil consequences of mismanagement of the circulation were palpable, and the legitimate profits which might be derived from the extension of a system of paper money in a country in which other means of economizing the use of coin had been so extensively established and were daily increasing, had become a matter of secondary consideration and even of trivial importance in a national point of view. It is, indeed, remarkable that the opponents of the Act of 1844 do not in general urge their objections from this point of view. They do not care for the legitimate profits to be derived from a well-managed

note circulation. Their indignation is aroused only when they contemplate the necessity which the Act imposes on banks of withholding accommodation when money is scarce, and when it is most sought for in consequence of that scarcity.

On these considerations it was decided that a strict limitation should be imposed on the issue of notes; that the circulation should be put on such a system that it must conform to the laws by which a metallic currency would be governed, as Mr. Tooke and Mr. Wilson say it ought to do, and even must do, and that the discretion of the Bank of England should be confined to its banking functions. The machinery established for this purpose is of the most simple character. The principle of a State circulation under defined regulations was adopted in place of a varying issue under the control of the Bank of England. A limited amount of notes is issued on the credit of public securities, and a restriction being placed, at the same time, on the amount of the issues of country banks, the quantity of notes circulating on credit is kept considerably within the amount of circulation which the country would require under the conditions of a metallic currency. Every note exceeding that limited amount is issued in exchange for bullion deposited, and the total amount of notes at any time in existence must, therefore, vary exactly in proportion to the variations in the quantity of bullion remaining in deposit. On considerations of convenience, the establishment already existing in the Bank for the assaying and refining of bullion, and the manufacture of notes, was maintained; but by the legal separation of the Issue from the Banking Department, subject to the regulations just described, all discretionary power over the issues of notes has been withdrawn from the Bank, as effectually as if the right of issue had been transferred to the Mint, or any other Department of the State. Under this regulation the Bank of England obtains, as a bank, the use of notes put in

circulation from the Issue Department by operations like those employed by any other bank. The notes constitute a paper-money, in every sense of the word, and that money is paid into the Banking Department of the Bank of England, or paid out of it, in precisely the same manner as it would receive or make payments in metallic money, if, instead of notes being issued in exchange for bullion, the gold were taken to the Mint and returned in the shape of coin.

The opponents of the Act of 1844 object to the separation of the Issue and Banking Departments of the Bank of England, and there are some among those who approve of a limitation of the issues on credit, who yet regard this separation as a cumbrous and unnecessary arrangement. They contend that the result would be precisely the same if the Bank were simply precluded from issuing more than a limited amount of notes, except on the deposit of bullion. There is no question that as regards the conduct of the business of the Bank this would be the case; but as regards the clear enforcement of a principle the effect would be very different. That principle was, that the quantity of notes and coin, combined, at any time in circulation should always be precisely the same as would be the quantity of coin alone, if notes did not exist. The working of this system could not be shown if notes were not created or cancelled, as bullion may be deposited or withdrawn, and the responsibility of the Bank of England in respect of its banking functions, when deprived of the function of regulating the issue of notes, would not clearly appear, if the accounts were still blended in the same form as was employed when the two functions coexisted.

Mr. Tooke once regarded this question in a different light from that which he now advocates. He expressed himself in the following terms on the subject of the separation of the business of issue from that of the ordinary business in the Bank of England, when the scheme

was first advocated by Mr. Jones Loyd (Lord Overstone):—

"The principle of such separate business of issue, so regulated, and constituting the only source of paper-money, is unquestionably the most scientific, the most simple, and the most secure against a suspension of cash payments, that can be adopted." *

Mr. Tooke qualified this recognition of a principle by suggesting whether there were not considerations of greater convenience in the working of the "less scientific system" which then prevailed. The acknowledgment of the perfection of the scheme, since adopted, for the working of a paper-money on a system according to which it would vary exactly as a metallic circulation would vary, is frank and explicit; but the qualifying considerations are not enunciated with equal clearness, as no attempt is made to show that, if the bullion were considered as the reserve both for the issues and the deposits, after a restriction had been imposed on the power of issue by the Bank, greater freedom would have been obtained in its action than that which it possesses under the regulation for the complete separation of the Departments, and that any convenience would therefore arise from the adoption of the suggestion. This cannot be shown, and the only effect of reuniting the Departments would be that obscurity which would be derived from confounding the operations of two distinct functions and which is conducive to erroneous speculation.

If any argument were wanting to show the wisdom of the measure of separating the functions of issue and banking, it would be afforded by the pertinacity with which the opponents of the Act of 1844 refuse to recognize the arrangement. The proposition is, that, if the issue of notes be kept distinct from the business of banking, and every note issued beyond a certain limit be issued only in

* Tooke on Prices, vol. iii, p. 250, 1840.

exchange for bullion, every note so issued is a certificate of value actually held in deposit and any day reclaimable, and the total amount of notes issued must vary with the amount of bullion in deposit. No proposition can be more plain or undeniable. It is evaded by mixing together the accounts of the Issue and Banking Department, and striking out of the account the reserve of notes held in the latter department. The whole train of sophistry which we have had under consideration hangs upon this expedient. The word "circulation" is applied by these writers, as we have observed already, to that portion only of the notes of the Bank of England which is in the hands of the public, excluding the reserve in the Banking Department. They then state that the scheme of the Act of 1844 is founded on the theory that a note circulation, as regulated by that Act, must fluctuate in amount, as a purely metallic currency would fluctuate; they prove by figures without end that the circulation, according to their limited acceptation of the term, does not so fluctuate, and they conclude that the theory of the Act is disproved. The answer to this reasoning is, that it is founded on a quibble about the interpretation of a word, which substitutes a part of the thing meant for the whole. The thing meant was, a note issued in exchange for bullion deposited in the Issue Department, and the aggregate quantity of notes issued from that department, which may be designated as circulation, paper-money, or any other name that may be agreed upon; and the theory was, that such aggregate quantity must vary with the amount of bullion deposited. Preserve the separation of departments, and that theory is worked out in a way that makes its truth palpable to any mind of ordinary capacity; revert to the old form of account, and that confusion must arise which is only favourable to fallacy.

Operation of the Act of 1844 in the year 1847.

The Act of 1844 was passed at a period of ease. It was soon put to the test of a severe ordeal by the return

of one of those cycles of excessive impulse in mercantile adventure to which all trading communities are subject. The opponents of the Act allege that, on this occasion, it not only failed in its object, but greatly aggravated the severity of the crisis which occurred in 1847.

In order to meet this allegation it is necessary to pass in review the events which led to the calamities of that year.

The year 1845 was one of unexampled prosperity. A long continuance of favourable exchanges had raised the bullion in the Bank to a higher amount than it ever reached before, exceeding at Midsummer 16,600,000*l.* A most abundant harvest, a large amount of floating capital seeking investment, and the freedom given to trade by the revision of the tariff, at the fortunate moment when the depression of the years following 1839 was passing away, all contributed to give an impulse to the spirit of speculation. Every branch of trade exhibited a tendency to unusual activity; but the extension of the railway system offered the most tempting inducements for investment, and the competition of rival companies and general eagerness to acquire shares in them, soon assumed the character of a mania. The effect of these investments in the rapid conversion of floating into fixed capital, and the consequent drain on the resources of the country, have been ably illustrated in some articles written by Mr. Wilson in the "Economist," early in 1847, and forming part of the series of papers collected in a volume to which allusion has already been made. A reaction was inevitable; but it was hastened and aggravated by the calamity of the failure of the potato crop in 1846, and the consequent necessity for immense importations of food.

Towards the end of 1846 the accounts of the Bank of England showed unequivocal symptoms of approaching pressure. The Bank, nevertheless, neglected to take precautionary measures. It continued to make advances at a

low rate of interest, although the general market rate had advanced. Its reserve, in consequence, underwent a rapid diminution, and the tardiness of its action aggravated the measures of restriction which it was at last obliged to adopt. The minimum rate of interest was raised from 3 to 3½ per cent. on the 16th of January, 1847, and to 4 per cent. in the following week. The pressure, however, still continued, and the reserve of notes was reduced on the 10th of April to 2,833,000*l.*, when the rate was raised to 5 per cent. This tardy action on the part of the Bank had the effect of producing a violent revulsion. The failure of houses which had become involved at this period would have been unavoidable, but the proceedings of the Bank increased the general pressure, and a crisis in the money market ensued. The "Economist" of the 1st of May, 1847, contained an article, written by Mr. Wilson, on the subject of this crisis, showing, by a convincing train of reasoning, that the difficulties in which the country was involved arose from the wild expenditure on railways, aggravated by the imperative necessity for importing large quantities of food; and, while the writer guarded himself in respect to his views on the general policy of the Act of 1844, he frankly avowed that the pressure of the time was not attributable to the operation of that Act, and he warned his readers that no permanent relief from further impending difficulties could be obtained, except through the means of strict economy and increased production.

These warnings were fully justified by subsequent events. The exchanges continued in an unfavourable state, but instead of any attempts to restrict expenditure a violent struggle was kept up by the railway companies to obtain the means of continuing their works. Commercial difficulties increased. At length, houses of great reputation gave way. The railway calls, and other demands for money, bore heavily on the deposits of banks; several banks, including the Royal Bank of Liverpool, which had

become involved by imprudent advances, stopped payment; increased pressure was imposed, in consequence, on the Bank of England; general distrust began to prevail, and those who had money hoarded it, in order to be prepared for unseen calamities; the reserve of notes in the Bank of England was reduced on the 23rd of October to 1,547,270*l.*, and a panic ensued. The celebrated letter of Lord John Russell and Sir Charles Wood suspending the operation of the Act of 1844, was issued on the 25th of October, and the panic was instantly allayed. The provisions of the Act were not actually violated. The panic proved to have been the result of vague apprehension, and when confidence was restored, it was found that there was no want of money for the legitimate objects of trade.

The object of the Act of 1844 was not to prevent those excesses and revulsions which are the common fruits of too great activity in trade, but to preserve the integrity of the paper money of the country. This effect was attained in 1847. But it has since been said that the calamities of that year might have been avoided or mitigated but for the stringency of the law, and that the great houses that failed in the autumn might have been saved by timely assistance. This is an appeal to the compassion of the public, which is calculated to make a deep impression on the unthinking. The calamities avoided are unknown, and if the relaxation of an abstract principle would have given relief, it seems hard that it should have been refused. On what ground however, is the assertion made? The only error that is attributed to the Bank of England in the management of its business in that eventful year, is the neglect to take early precautions at the commencement of the pressure; it then erred on the side of laxity. Its subsequent proceedings evinced great prudence, and Mr. Wilson, in the article in the "Economist" which has been referred to, contended earnestly for the necessity for the maintenance

of that reserve of gold which, under the operation of the Act, remained in the Bank throughout the period of pressure. The testimony of Mr. Wilson on this point is of great value. Whatever opinion may be entertained of the correctness of some theoretical doctrines which he has advocated, no one has clearer perceptions of the practical application of sound principles; and, in his judgment, the management of the circulation in the summer of 1847, under the Act of 1844, was precisely what it ought to have been if no restrictions had been imposed on the Bank. If this be the case, it is not easy to see by what means assistance could properly have been extended to the houses which failed. Relief could only have been afforded to them by advances of notes, and it is admitted that, even if the law would have permitted it, additional notes ought not to have been issued.

Truth, however, demands that the title of those houses to expect relief should be shown, before the appeal *ad misericordiam* in their behalf can be admitted. The proceedings in bankruptcy disclosed the fact that merchants who stood high in the world had been for years insolvent, and had been carrying on the most improvident speculation. A system was found to have been long in operation of purchasing commodities on credit, not with a view to legitimate gain, but for the purpose of discounting bills procured by the resale of the merchandise so obtained. Production was thus increased beyond the real demand, and the transactions were not only injurious to those who were immediately connected with these houses, but to the prudent and honest merchant, who was deprived of his fair profits by competition with these reckless traders. Is it for houses of this character that our sympathy is to be excited? It is probable that in the wreck which ensued, some persons were involved against whom no imputations of unfair dealing, or even rash speculation, would justly apply; but looking to the general character of the failures

of that period, it cannot be said, with any regard to propriety, that any of the firms which suspended payment possessed such claims to sympathy as to entitle them to relief by a proceeding which would have exposed the whole community to loss and inconvenience.

It is contended upon no light grounds that national discredit would have been the consequence of an extension of the paper circulation in 1847; and if speculative opinions are indulged in unfavourable to the Act of 1844, with reference to calamities which are thought to be traceable to its operation, it is allowable, on the other hand, to show the additional calamities which would have ensued if the restraints of the Act had not existed.

We have referred to the effects of the railway speculations of 1845 and 1846, in disturbing the ordinary channels of trade, and the contentions in the money market, on the part of those who were involved in these undertakings, to obtain the means of carrying them on, when the pressure of 1847 was at its height. At that period the most ridiculous notions were entertained by many, who might have been expected to have been better acquainted with the theory of money, regarding supposed requirements for an increased circulation; and schemes were submitted to the Government for the creation of a new description of paper money, to be issued on the credit of Exchequer Bills, or other public securities, and to be made specially applicable to the expenses of railway works. These may be said to be the emanations of the unsettled minds of wild speculators. But a more imposing demonstration was made by the merchants, traders, and bankers of London in a petition presented to the House of Commons on the 13th of July, 1847, averring that there was "no undue extension of the ordinary commerce of the country, or any spirit of speculation or over-trading afloat, so far as the trading interest was concerned," and praying for a relaxation of the provisions of the Act of 1844.

Similar views were advocated in the House of Commons by Mr. Thomas Baring, in a speech which made that deep impression which opinions coming from a person of high commercial reputation, and advocated with great ability, were calculated to convey.

When such opinions prevailed throughout the country, when we regard the difficulties in which several banks were involved in consequence of the pressure of the times, and the disposition shown by the Bank of England, in the early part of the year, to be too free in its accommodation, can we doubt that the country banks, if they had had the power, would have yielded, as on former occasions, to the temptation of over-issue: and can we in reason suppose that the Bank of England, if unsupported by the stringency of the law, would have been able to withstand the general pressure for extended accommodation which would have been brought to bear upon it? No; the Act of 1844 is not responsible for the calamities of 1847. On the contrary, it saved the country from a collapse like that which followed the crisis of 1839. If any one doubts this, let him refer to the slow reinstatement of the prosperity of the country after the prolonged drain upon its resources at the last-mentioned period, and contrast with it the speedy recovery from the distress of 1847 after the scum of insolvency had been swept away.

It is not surprising that, on the first ordeal through which the Act of 1844 passed, the mercantile community should have been influenced by grave fears regarding its operation at a time of great and accumulated difficulty. So far as the pressure arose from recent excitement in trade, the consequences of wide-spread speculation on former occasions in our commercial history might have afforded a guide to thinking men. The crisis was, however, peculiar in many respects. The effects of the railway mania were palpable; the difficulties of the corn trade

in the early part of the year were attributable to known causes; but the failures in the autumn of 1847 involved houses of extensive business and reputed wealth, whose speculations had not originated in prevailing and temporary excitement, but were of long standing, and had no other connection with the special circumstances of the time, than that their embarrassments were brought to light and probably precipitated by the general pressure on the money market. A general feeling of anxiety arose in consequence. No one knew whom to trust. At the approach of difficulty an impression widely prevailed that it would be aggravated by the stringency of the Act of 1844, and, when the crisis came, the community felt themselves left to their own resources, and, for the first time, deprived of that resort to the Bank of England on which habit had taught them to place a weak dependence. The law of human nature, "omne ignotum pro terribile," operated strongly upon them. Mutual confidence had left them, and with it all power of concert. Mercantile men came to the Government in this strait, but not for money. Sir Charles Wood, in his speech on the 30th November, 1847, detailed the nature of the applications made to Lord John Russell and himself. They were simply for a relaxation of the provisions of the Act, with the view not of obtaining bank notes, but a restoration of confidence. Their words were, "We do not want notes, but give us confidence. We have notes enough, but we have not confidence to use them; say that you will stand by us, and we shall have all that we want; do anything, in short, that will give us confidence. If we think we can get notes we shall not want them. Charge any rate of interest you please, ask what you like."* The result proved the correctness of their anticipations. When authority was given for relaxing the Act, confidence was

* Speech of the Chancellor of the Exchequer, November 30, 1847. Hansard's Debates, third series, vol. xcv.

immediately restored. The panic was occasioned not by the operation of the law, but by vague, unreasoning, and unfounded apprehensions of its effect.

But it is still urged by some that the panic was occasioned by the knowledge that the Bank of England, though possessing gold in its coffers, could not use it for the benefit of trade; and they hence conclude that the restriction imposed by the Act was unnecessary because it came into practical effect when the Bank had possession of ample means, and was injurious because it destroyed confidence when, as the event showed, the Bank would not have been called upon to have exercised prejudicially any discretion with which it might have been entrusted. It is manifest, however, that we cannot surely predicate what might have happened under supposed circumstances, from events which occurred under different conditions. The previous history of the Bank does not warrant the supposition that it would have imposed a timely check on the downward course in 1847, if its discretion had been unfettered. All we know, for certain, is that the measures, which the Act of 1844 rendered it necessary for it to adopt, in the autumn of 1847, were beneficial in themselves, and did not in their results justify the alarm which they excited.

When a monetary difficulty arises in consequence of excessive speculation, over-trading, or other circumstances causing a greater demand for floating capital than the resources of the country can at the time supply, a check on expenditure must necessarily be applied at some period by restricting the use of credit. If no other limit be imposed, it will occur in the natural course of events by the process of exhaustion. The question at issue regards the time at which it is most beneficial for the country at large that the check should be applied. The Act of 1844 requires that it should be applied before the resources of the Bank itself are endangered, and in the expediency of

this object, sound and thinking men of all parties practically concur. The most enlightened opponents of the Act of 1844 themselves hold the opinion that an ample reserve of bullion ought at all times to be maintained; they cannot show that this desirable object can be secured under any system which leaves a power of discretionary issue; and they cannot show that, if reliance could be placed on such discretionary power, its operation, if effectual for the object of arresting a drain of bullion by timely restraint, would be less felt by those who look for help, or would cause less immediate pressure, than the enforced action imposed by the Act of 1844.

Times may come in which the commercial relations of the country may be placed, as they have been before, in so anomalous a position as to demand the interference of the State; but it would be unreasonable to conclude that, because the Government thought it right to interpose in 1847, the system established in 1844 cannot, and ought not to be maintained. As well might it be urged that, because cash payments were suspended under the pressure of a State necessity in 1797, the principle of convertibility was proved to be unsound, and ought never to have been resumed.

Operation of the Act of 1844 in the years 1855 and 1856.

Lord Overstone, in his evidence before the Commons' Committee on the commercial distress of 1847, expressed an opinion that the experience derived from the events of that year would rectify mistakes which had occurred on the first occasion of difficulty and trial to which the new system had been exposed, and that the importance of looking into the state of the Bank reserve would thenceforward be better understood, both by the Bank and the public. This prediction has been fully verified by the working of the system under the pressure arising from the late war, and the excitement and speculation consequent on the return of peace. During the two last years the com-

mercial interests of the country have been exposed to severe trial. In 1855 a continued drain of bullion, occasioned by the most wasteful and unproductive of all expenditure, ordinary channels of trade closed, and, to crown all, the calamity of a deficient supply of corn, owing to the principal sources for the supply of foreign corn having been cut off, these constituted an accumulation of difficulties which filled the minds of all thinking men with apprehension. Every element of commercial pressure was present, with the exception in favour of this country of the absence of disturbing effects from undue speculation. This pressure was not confined to the United Kingdom; it prevailed throughout the continent of Europe and in America. In the United States extensive failures of banks occurred, deranging the circulation of many districts. In Prussia it became necessary to adopt stringent measures to correct the effects of over-issues of paper by the banks. The currency of other countries where paper money is extensively used was exposed to similar derangement. But the pressure necessarily bore with greater severity on those countries which were actually engaged in war; yet, for the first time since the suspension of cash payments in 1797, great financial difficulties were overcome without derangement of our currency. The return of peace did not bring with it the relief that was expected. After a reduced rate of interest had prevailed for some months, renewed pressure arose from the demand for capital for transmission to the continent, partly in consequence of great extension of speculation, and partly owing to the derangement of the monetary system of most European countries from the conflicting operation of increased supplies of gold, and of extraordinary demands for silver for shipment to the East. The Bank of England, in order to counteract the drain of bullion, was obliged to resort to the measure of raising its minimum rate of discount even above the rate which had prevailed at the latter period of

the war, and to take other stringent measures with regard to advances on stock. Still the general trade of the country remained in a sound and healthy state. No violent revulsion took place, and the principal failures or suspensions which occurred were either those of banks, whose fraudulent and reckless proceedings are the theme of universal indignation, or of firms which, though affording subject of regret on account of their respectability, had embarked in undertakings clearly exceeding the limits of available capital. The prudence with which trade has generally been conducted and the soundness of credit are doubtless the cause of this satisfactory state of things; and though this healthy condition can only be attributable in a secondary degree to the influence of the Act of 1844, it may yet be affirmed with confidence that, but for the operation of that Act, the Bank would have been unable to maintain the prudent course of action by which this great result was secured.

The period has now arrived at which the constitution of the Bank of England may be revised by Parliament, and there is a general impression that a full inquiry into the subject will be undertaken next year. The time is favourable for dispassionate investigation, as ample experience has been afforded of the working of the system established in 1844, and the question can be approached free from those prejudices which generally arise from the weight of recent disaster or present difficulty. There is wide matter for consideration, as the inquiry may be extended to the constitution of the Bank of England itself, and its position in connection with the Government of the country, as well as to the peculiar functions which are discharged by it in relation to our monetary system. But the two branches of the subject are distinct. The former involves questions of State policy to be considered only on grounds of expediency; the latter involves ques-

tions of fundamental principle with which the institution of the Bank of England itself has only a subsidiary connection.

The objections urged against the system of currency established in 1844 have hitherto been founded on speculative opinions opposed essentially to the theory of money as defined by the greatest writers on political economy, or on vague suggestions of expediency which, so far as they come from writers of any weight, are hesitatingly and inconsistently enounced. It behoves those who consider that some regulations are necessary for the preventing abuses in the issue of bank notes, and yet object to the provisions of the Acts of 1844 and 1845, to define the system which they would recommend for adoption. Until that be done, we have a right to conclude that their practical views are as uncertain as their theoretical opinions are unsound.

Other objections may be urged against the Acts, on the ground that they are based on a principle of State control which is not fully carried out, and that, in regard to the issues of the country notes in England, and to the circulation of Ireland and Scotland, the existing arrangement has the incompleteness of a compromise. These are fair subjects for inquiry.

The arrangement of 1844 was avowedly founded on an adaptation of existing institutions to principles derived from experience, rather than on abstract theory. The measure was one of restriction, not of construction. It is possible that a better and more complete scheme may be devised. But we shall be dealing with a question connected with a refined and complicated system of credit, which has grown with the experience of the community, and is identified with, and adapted to, the business habits of the people. We are embarked on times in which great experiments are in progress for extending the facilities afforded by that system of credit, and the monetary basis on which

the whole must rest will necessarily have a considerable influence on the success of those measures. There is, therefore, peculiar ground for caution before we attempt to disturb the existing system of currency. It would be folly to take a retrograde step, unless it be proved to demonstration that the measure has worked ill, and hardly less so to pull down for the sake of reconstruction, unless we are assured that those who criticise the existing fabric are sound and consistent in their own views, and have the capacity to improve what may be defective, without exposing the credit of the country to the risk of an ill-contrived and imperfect substitute.

APPENDIX.

YEARLY AVERAGES of Bank of England Notes held by the public since 1844; showing by the variation in the different denominations, the saving effected, by certain banking arrangements, in the total circulation.

	A. £5 to £10.	Per Centage of Circulation.	B. £20 to £100.	Per Centage of Circulation.	C. £200 to £1,000.	Per Centage of Circulation.	Total.	London.	Country.
	£ m.		£ m.		£ m.		£ m.	£ m.	£ m.
1844	9.263	45.7	5.735	28.3	5.253	26.0	20.241	14.214	6.027
1845	9.698	46.9	6.082	29.3	4.942	23.8	20.722	13.927	6.795
1846	9.918	48.9	5.778	28.5	4.590	22.6	20.286	13.759	6.527
1847	9.591	50.1	5.498	28.7	4.066	21.2	19.155	12.892	6.263
1848	8.732	46.9	5.046	29.5	4.307	23.8	18.085	12.498	5.587
1849	8.692	47.9	5.234	28.6	4.477	24.3	18.403	12.796	5.607
1850	9.164	47.2	5.587	28.8	4.646	24.0	19.398	13.433	5.965
1851	9.362	48.5	5.554	28.5	4.557	23.0	19.473	13.403	6.070
1852	9.839	45.0	6.161	28.2	5.856	26.8	21.856	15.281	6.575
1853*	10.699	47.3	6.393	28.2	5.541	24.5	22.633	15.274	7.359
1854†	10.565	51.0	5.910	28.5	4.234	20.5	20.709	13.626	7.083
1855‡	10.628	53.6	5.706	28.9	3.459	17.5	19.793	12.751	7.042

* In July, 1853, the Joint Stock Banks and the private Banks paid each other by drafts upon the Bank of England instead of by Bank Notes.

† In May, 1854, the balances of the clearing house were settled by transfer drafts upon the Bank, and Joint Stock Banks were admitted to the clearing shortly after.

‡ In April, 1855, the customs' duties were paid by transfer drafts; since that time 69,000 payments have been made in that way.

N.B.—The foregoing figures represent millions, the three final cyphers being omitted.